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ENTERPRISE ZONE PROGRAM AND ITS IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT

HEARINGS

BEFORE THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

ENTERPRISE ZONE PROGRAM AND ITS IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT

JUNE 21 and SEPTEMBER 21, 1989

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ENTERPRISE ZONE PROGRAM AND ITS IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT

JUNE 21, 1989

U.S. SENATE,
COMMITTEE ON SMALL BUSINESS,*
Washington, DC.

The Committee met, pursuant to notice at 9:40 a.m. in room SR-428A Russell Senate Office Building, Hon. Joe Lieberman and Hon. Rudy Boschwitz (Acting Chairmen) presiding.

STATEMENT OF HON. JOSEPH I. LIEBERMAN, A U.S. SENATOR FROM THE STATE OF CONNECTICUT

Senator LIEBERMAN. This hearing will come to order. I am pleased to welcome everyone to this Small Business Committee hearing on Enterprise Zones and pleased particularly to be co-chairing this in the spirit of true bipartisanship and equality with my friend and colleague from Minnesota, Senator Rudy Boschwitz. I am very proud to join Senator Boschwitz as a co-sponsor of his Enterprise Zone legislation in the Senate this year.

As I guess most of you know, by an announcement was made earlier, Secretary Kemp was called to the White House this morning. I received a call from him. I know you are disappointed. I can see faces grow elongated over here. He will return on another occasion to speak with us and advocate Enterprise Zones, for which he has been an early and consistent supporter here in the United States.

We do have two outstanding panels of State and local experts and administrators who have been involved with Enterprise Zone legislation and I hope this hearing therefore can be a good beginning for the dialogue about Enterprise Zones.

As most of you probably know, the concept of Enterprise Zones has been around for some time too. Englishmen of diverse political philosophies, Peter Hall and Sir Geoffrey Howe, first began working on this idea in the 1970s. It came to fruition in England in 1980, when an Enterprise Zone Program was enacted by Prime Minister Thatcher and her Government.

The first Enterprise Zone legislation on a national level in this country was introduced by two Members of Congress who are also of diverse orientation, Representative Jack Kemp, then Congressman, a Republican from Buffalo, NY, and Representative Bob Garcia, a Democrat from the south Bronx.

What brought these two men together was clearly a desire to find a long-term solution to poverty while stimulating economic de-

velopment across our Nation. Finally, in 1987, during the 100th Congress, the Enterprise Zone legislation was passed into law as part of an omnibus housing bill.

In essence, this bill directed the Secretary of Housing and Urban Development to designate 100 Enterprise Zones across the country, but it did not provide for any corresponding Federal tax benefits. That is what the bill that Senator Boschwitz has introduced, and which I am proud to co-sponsor, would do.

It would put into place taxing centers, which are really the nuts and bolts of Enterprise Zones, or as someone else said, it would put the engine into the car of Enterprise Zones. This bill attempts to bring benefits to impoverished urban and rural areas without incurring an overall loss of revenue.

At the same time, I think it is important to look beyond statistics as we measure the impact and consider the social and economic impacts that this program can have in a community by giving its residents jobs and a new sense of hope about their future.

The Federal Government cannot act alone in tackling the problems of our inner cities and poor rural areas. We must obviously work with business and industry to develop a strategy that will attack chronic poverty I must say that that is the most appealing feature of Enterprise Zones to me, is the attempt to involve the private sector in doing something substantial on a national scale about chronic poverty.

Poverty not only encompasses whole sections of every one of our inner cities, it also, in too many cases, spans generations and therefore clouds our Nation's future. The unemployed and the hopeless, whether they are in the Bronx, or Bridgeport, or East St. Louis, or Watts, or Liberty City, are a problem for all of us and Enterprise Zones, I believe, offer one innovative solution to that problem.

Senator LIEBERMAN. I look forward to the testimony today and I am pleased now to yield the gavel in the spirit of bipartisanship to Senator Boschwitz.

[The prepared statements of Senator Lieberman and Senator Dixon follow:]

JOSEPH I. LIEBERMAN
CONNECTICUT

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OPENING STATEMENT FOR ENTERPRISE ZONE HEARING

Senator Joseph I. Lieberman

I want to welcome everyone to the Small Business Committee's hearing on Enterprise Zones. I am pleased to be here today with my friend and colleague from Minnesota, Sen. Rudy Boschwitz, who I am proud to join as cosponsor of enterprise zone legislation in the Senate.

The concept of enterprise zones has been around for some time. Two Englishmen of diverse political philosophies, Peter Hall and Sir Geoffrey Howe first began working on this idea in the 1970s. It came to fruition in 1980, when an enterprise zone program was enacted by Prime Minister Thatcher.

The first enterprise zone legislation in this country on the national level was introduced by two Members of Congress also of diverse background, Rep. Jack Kemp, a Republican from Buffalo New York, and Rep. Bob Garcia, a Democrat from the South Bronx, while Jimmy Carter was still President. What brought these two men together was a desire to find a long term solution to poverty while stimulating economic development across our nation.

Finally, in the 100th Congress enterprise zone legislation was passed into law as part of an omnibus housing bill. In essence, this bill directed the Secretary of Housing and Urban Development to designate 100 enterprise zones across the country, but it did not provide for any corresponding federal tax benefits. That is what the bill which Sen. Boschwitz and I have introduced would do: put into place those tax incentives which are considered to be the nuts and bolts of enterprise zones.

Our bill attempts to bring benefits to impoverished urban and rural areas without incurring an overall loss of revenue. At the same time, it is important to look beyond statistics and consider the positive social impact that this program can have on a community by giving its residents a new sense of hope about their future.

It is clear to me that the federal government cannot act alone in tackling the problems of our impoverished inner cities and rural areas. We must work with business and industry to

and rural areas. We must work with business and industry to develop a strategy that will attack chronic poverty. Most states have begun to do precisely this by establishing their local versions of enterprise zones.

The most appealing feature of enterprise zones is their attempt to involve the private sector in doing something substantial on a national scale about chronic poverty. Poverty that not only encompasses whole sections of every one of our inner cities but also in, too many cases, spans generations and is a cloud over our nation's future. The unemployed and the hopeless, whether they are in the Bronx, Bridgeport, East St. Louis, Watts, or Liberty City are a problem for us all. Enterprise zones offer one innovative solution to that problem.

-30-

JULY 21, 1989

STATEMENT OF SENATOR ALAN DIXON

SMALL BUSINESS COMMITTEE HEARING
ON
ENTERPRISE ZONE PROGRAMS AND THEIR IMPACT
ON SMALL BUSINESS GROWTH AND DEVELOPMENT

MR. CHAIRMAN, I AM PLEASED TO BE HERE THIS MORNING AS THE SENATE SMALL BUSINESS COMMITTEE REVIEWS ENTERPRISE ZONE PROGRAMS AND THEIR IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT. WE HAVE A DISTINGUISHED GROUP OF WITNESSES BEFORE US THIS MORNING. I KNOW THE COMMITTEE WILL FIND THEIR TESTIMONY TO BE INFORMATIVE AND HELPFUL.

I WANT TO TAKE THIS OPPORTUNITY TO WELCOME MY DISTINGUISHED HOUSE COLLEAGUE, MARY ROSE OAKAR, TO THE COMMITTEE. I KNOW HOW MUCH TIME AND ATTENTION CONGRESSWOMAN OAKAR HAS GIVEN TO THE ENTERPRISE ZONE ISSUES. I APPRECIATE HAVING THE BENEFIT OF HER EXPERTISE AND ADVISE.

I DO NOT WANT TO TAKE THE TIME OF THE COMMITTEE TO MAKE A LONG OPENING STATEMENT. INSTEAD, I WOULD SIMPLY LIKE TO POINT OUT THAT I AM A LONG-TIME SUPPORTER OF ENTERPRISE ZONES AND THAT I BELIEVE THAT SMALL BUSINESSES ARE THE KEYS TO SUCCESS OF ANY ENTERPRISE ZONE PROGRAM. I LOOK FORWARD TO WORKING WITH TODAY'S WITNESSES AND ALL OTHER INTERESTED PARTIES IN AN EFFORT TO IMPROVE FEDERAL ENTERPRISE ZONE INCENTIVES.

ENTERPRISE ZONES REPRESENT A REAL ECONOMIC PROMISE TO ECONOMICALLY DISTRESSED AREAS SUCH AS IN MY OWN STATE OF ILLINOIS, AND ACROSS OUR NATION. WITH THE RIGHT KIND OF REFORMS AND IMPROVEMENTS, WE CAN ENSURE THAT THE FULL POTENTIAL OF ENTERPRISE ZONES IS REALIZED. OUR SESSION TODAY WILL GIVE THIS COMMITTEE THE OPPORTUNITY TO GAIN INSIGHT AS TO HOW A SUCCESSFUL FEDERAL ENTERPRISE ZONE PROGRAM MAY BEST BE DEVELOPED.

I WELCOME THE DISTINGUISHED WITNESSES BEFORE US, AND LOOK FORWARD TO HEARING THEIR TESTIMONY. THANK YOU, MR. CHAIRMAN.

STATEMENT OF HON. RUDY BOSCHWITZ, A U.S. SENATOR FROM THE STATE OF MINNESOTA

Senator BOSCHWITZ. Thank you very much, Senator. Your statement is fairly close to mine in the sense that we are here for the same reason and have the same ideas with respect to Enterprise Zones and I am indeed pleased to have you as the co-sponsor of our bill. I, too, regret that Secretary Kemp cannot be with us this morning. I think that there are some conflicts going on within the Administration as to what should be said about Enterprise Zones at this juncture. Secretary Kemp, being a very firm advocate of Enterprise Zones, more so than some of his colleagues in the Administration, is finding it difficult to be as outspoken about them as he wants to be this morning and the result is that we are going to have to have him on another day. We will do that; he wants to come up and do that as well.

The Senator from Connecticut really has outlined the purpose of Enterprise Zones and has given some of the history.

We did approve the measure in conjunction with the HUD reauthorization that provides for Enterprise Zones. In that measure, it was determined that one third of the zones would be rural. Since I am also on the Agriculture Committee and have taken quite an interest in rural legislation to deal with rural poverty and rural development, I am particularly pleased with that element of it.

My State, unlike my friend from Connecticut, is a very large one. As a matter of fact, as large as all of New England and New Jersey and Maryland thrown in, so we have rural areas that really are far from places of employment growth and therefore that element of the bill is particularly important to us.

There have been various measures proposed to attack this Nation's social and economic ills. Traditionally we have chosen to spend large sums of money to resolve the problem of economic blight through the creation of welfare institutions.

Today, welfare obligations absorb large parts of the Federal budget. Admittedly some of those programs provide crucial services to the most distressed in our population, but on their own they do not and have not achieved the results we need to raise the living standards of all Americans.

Frankly, the present system has trapped many of our poor in a self-perpetuating cycle of poverty instead of offering a chance to free themselves and their families from this condition.

The impact of joblessness is painfully evident, and the difficulty of creating jobs in the areas that we would call Enterprise Zones is very apparent. Thus, the legislation with respect to this was started, as my friend from Connecticut pointed out, in the House by Congressman, then Congressmen Kemp and Garcia.

Here in the Senate, I introduced the first Enterprise Zone bill in 1980 which was a companion bill to those in the House. It passed a couple of times, but was dropped in conference. We now have made a little progress by at least getting the Enterprise Zones without teeth, so to speak, put into a HUD bill that passed in 1987.

Regretfully, we have to do things in Congress bit by bit, step by step. Sometimes I like to have a sense, as in business, that you can go from point A to point B in a relatively uninterrupted pattern.

But, one of the adjustments I have had to make getting into the legislative process is that it very seldom happens that way unless it involves football games on TV or something. Then we do it quickly. More meaningful legislation takes time.

But, State and local governments have beat us to the punch and have moved along much faster. Presently, 36 States and the District of Columbia have adopted Enterprise Zone programs. In 1987, in my own State of Minnesota, for example, 877 businesses distributed among 24 Minnesota cities were awarded tax credits under a State funded Enterprise Zone Program.

Local authorities estimate that 1,440 jobs were created, of which 864 were filled by economically disadvantaged people. Under the Minnesota plan, State-paid tax credits are allowed for business expansion, or new business investment, including a property tax credit for a portion of new eligible business in the zone, an income tax credit to partly offset the cost of debt financing, an income tax credit to employers for each additional worker employed in the zone, and an exemption from general sales tax on construction materials or equipment purchased for use in the zone.

Those are very powerful things. When you consider the elements that are in the bill that Senator Lieberman and I introduced and then also include some of the things that I have just outlined in the Minnesota plan, you really can give some meaningful advantages to business and get them—kind of jump-start them into Enterprise Zones.

So I am pleased that we have such a distinguished panel—two panels—this morning, for the purpose of reviewing this subject. I am sorry that the Secretary of HUD cannot be here, but he will be here and I thank you, Mr. Chairman and return to the Senator from Iowa.

[The prepared statement of Senator Boschwitz follows:]

STATEMENT OF SENATOR RUDY BOSCHWITZ

FOR THE

SMALL BUSINESS COMMITTEE HEARING ON

ENTERPRISE ZONES

6/21/89

I WANT TO BEGIN BY WELCOMING OUR PANEL OF DISTINGUISHED WITNESSES WHO HAVE TAKEN TIME FROM THEIR SCHEDULES TO TESTIFY ON THE ISSUE OF ENTERPRISE ZONES AND THEIR IMPACT ON SMALL BUSINESS. TO THOSE WHO HAVE TRAVELED LONG DISTANCES TO APPEAR FOR THESE PROCEEDINGS, I AM JOINED BY MY COLLEAGUES IN EXPRESSING SPECIAL APPRECIATION.

THERE HAVE BEEN VARIOUS MEASURES PROPOSED TO ATTACK THIS NATION'S SOCIAL AND ECONOMIC ILLS. TRADITIONALLY, WE HAVE CHOSEN TO SPEND LARGE SUMS OF MONEY TO RESOLVE THE PROBLEM OF ECONOMIC BLIGHT THROUGH THE CREATION OF WELFARE INSTITUTIONS. TODAY, WELFARE OBLIGATIONS ABSORB NEARLY HALF THE FEDERAL BUDGET. ADMITTEDLY, SOME ANTI-POVERTY PROGRAMS PROVIDE CRUCIAL SERVICES TO THE MOST DISTRESSED IN OUR POPULATION. BUT, ON THEIR OWN, THEY DO NOT APPEAR TO ACHIEVE THE RESULTS WE NEED TO RAISE THE LIVING STANDARDS OF ALL AMERICANS. FRANKLY, THE PRESENT SYSTEM HAS TRAPPED MANY OF OUR POOR IN A SELF-PERPETUATING CYCLE OF POVERTY INSTEAD OF OFFERING A CHANCE TO FREE THEMSELVES AND THEIR FAMILIES FROM THIS CONDITION.

THE IMPACT OF JOBLESSNESS IS PAINFULLY EVIDENT. DRUG ABUSE AND CRIME ARE ON THE RISE. INSTITUTIONS SUCH AS FAMILIES, SCHOOLS AND CHURCHES WHICH FORMERLY IMBUED OUR CHILDREN WITH PRODUCTIVE VALUES ARE CRUMBLING BEFORE OUR EYES. IN SPITE OF THE GENERAL ECONOMIC RECOVERY, WE ARE LEARNING THAT WHEN WE FAIL TO INSURE THAT ALL CITIZENS HAVE A SHARE IN THIS RECOVERY, WHEN WE TURN OUR BACKS ON AN UNEDUCATED, IMPOVERISHED LOWER CLASS, THE PRICE IS ULTIMATELY EXACTED AGAINST THE WHOLE OF SOCIETY. PAYING THIS PRICE WILL REDUCE OUR ABILITY TO COMPETE IN THE WORLD ECONOMY.

HOW, THEN, DO WE COMBAT JOBLESSNESS AND POVERTY? ONE MEANS IS THROUGH ENTERPRISE ZONES, A CONCEPT THAT DEALS WITH JOBLESSNESS AND ECONOMIC IMPOVERISHMENT BY ENLISTING THE HELP OF THE PRIVATE SECTOR. ENTERPRISE ZONES WOULD ENCOURAGE JOB CREATION THROUGH A FEDERAL/STATE/LOCAL PACKAGE OF TAX BENEFITS AND OTHER INCENTIVES OFFERED TO BUSINESSES THAT LOCATE OR EXPAND OPERATIONS IN A DESIRED ZONE.

IN THE SENATE, LEGISLATION ON ENTERPRISE ZONES HAS BEEN EVOLVING SINCE THE BEGINNING OF THE DECADE. MY URBAN JOBS AND ENTERPRISE ZONE ACT OF 1980 AND THE HOUSE COMPANION BILL INTRODUCED BY MY GOOD FRIEND JACK KEMP, WERE THE SEED FROM WHICH THE ENTERPRISE ZONE IDEA GREW. THE FULL SENATE PASSED MY ENTERPRISE ZONE BILL IN 1983 AND IN 1984. UNFORTUNATELY, BOTH TIMES IT WAS DROPPED BY THE CONFERENCE COMMITTEE.

MORE RECENTLY, IN 1987, THE HOUSING AND COMMUNITY DEVELOPMENT ACT WAS ENACTED INTO LAW. TITLE VII OF THE ACT PROVIDES FOR THE ESTABLISHMENT OF 100 ENTERPRISE ZONES, ONE-THIRD OF THEM IN RURAL AREAS. WHILE THE ACT ALLOWS THE SECRETARY OF HUD TO WAIVE REGULATORY RESTRICTIONS AND LOCAL AND STATE GOVERNMENTS TO TRANSFER MONEY FROM OTHER SOURCES TO THESE ZONES, IT DOES NOT PROVIDE ANY FEDERAL INCENTIVES TO COMPLEMENT LOCAL INITIATIVES. MY ENTERPRISE ZONE IMPROVEMENTS ACT OF 1989 CALLS FOR FEDERAL INCENTIVES IN THE FORM OF TAX CREDITS FOR EMPLOYERS AND EMPLOYEES IN BUSINESSES LOCATED WITHIN A DESIGNATED ENTERPRISE ZONE.

STATE AND LOCAL GOVERNMENTS HAVE ALREADY EXHIBITED REMARKABLE ENTHUSIASM FOR THE ENTERPRISE ZONE CONCEPT. PRESENTLY, THIRTY-SIX STATES AND THE DISTRICT OF COLUMBIA HAVE ADOPTED ENTERPRISE ZONE PROGRAMS. IN 1987 IN MY OWN STATE OF MINNESOTA, FOR EXAMPLE, 877 BUSINESSES DISTRIBUTED AMONG 24 MINNESOTA CITIES WERE AWARDED TAX CREDITS UNDER A STATE FUNDED ENTERPRISE ZONE PROGRAM. LOCAL AUTHORITIES ESTIMATE THAT 1,440 JOBS WERE CREATED, OF WHICH 863 WERE FILLED BY ECONOMICALLY DISADVANTAGED PEOPLE. UNDER THE MINNESOTA PLAN, STATE-PAID TAX CREDITS ARE ALLOWED FOR BUSINESS EXPANSION, OR NEW BUSINESS INVESTMENT, INCLUDING A PROPERTY TAX CREDIT FOR A PORTION OF A NEW ELIGIBLE BUSINESS IN THE ZONE, AN INCOME TAX CREDIT TO PARTLY OFFSET THE COST OF DEBT FINANCING USED TO CONSTRUCT NEW FACILITIES, AN INCOME TAX CREDIT TO EMPLOYERS FOR EACH ADDITIONAL WORKER EMPLOYED IN THE ZONE, AND AN EXEMPTION FROM GENERAL SALES TAX ON

CONSTRUCTION MATERIALS OR EQUIPMENT PURCHASED FOR USE IN THE ZONE.

I WOULD LIKE TO CONCLUDE BY SAYING THAT I LOOK FORWARD TO TODAY'S TESTIMONY. YOUR COMMENTS AND IDEAS ARE CRUCIAL TO OUR FORMULATING EFFECTIVE ENTERPRISE ZONE LEGISLATION. IT IS A FRESH, PROMISING APPROACH TO DEALING WITH PROBLEMS OF STRUCTURAL UNEMPLOYMENT AND REVITALIZING DISTRESSED AREAS IN OUR NATION'S CITIES AND RURAL TOWNS.

Senator GRASSLEY. Thank you, Mr. Chairman.

Senator BAUCUS. Mr. Chairman, just briefly. I have to Chair a hearing at 10 o'clock.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM THE STATE OF MONTANA

Senator BAUCUS. I would just like to very briefly say how much I believe this issue is very critical to many parts of America. It was not too many years ago—about 130 or so years ago—that a great American President, Abraham Lincoln, during a very divided period in this country's history, very wisely noted that a country divided cannot stand. A country divided falls.

He helped to bring our country together at that time—a very tragic time in our country's history, but nevertheless an effort that was necessary to bring our country together. Today we are not engaged in a time when our country is divided North against South or East versus West.

In many respects we are divided urban versus rural, and urban Enterprise Zones are very helpful to provide economic growth and development to urban—necessary parts of urban America. It is equally true we need rural Enterprise Zones, because this country is now pitted to a large degree, urban versus rural.

As you know, Mr. Chairman, the Majority Leader appointed a Task Force to address rural economic development. That is proceeding very expeditiously, but at the same time there are components of that which I think can be refined and developed further—namely, Rural Enterprise Zones.

Essentially the problems of rural America, in my view, stem from excessive deregulation in the 1980s, transportation deregulation, airline, bus and rail, financial services, to some degree medical deregulation, telecommunications deregulation. The effects obviously are to help urban parts of America, the more congested parts of America, at the expense of, and hurt, rural parts of America. It is something that has to be addressed.

I think that rural Enterprise Zones will help address that and it is incumbent upon us as a country to remember that we have to stand together.

Our national motto is E Pluribus Unum—one out of many. I think in the 1980s there has been too much emphasis on the Pluribus and not enough attention on the Unum. We have got to spend more time together as a country, a single country where we help each other out and the more we do, the more we are going to find that our common standards of living will rise more quickly for more Americans.

I think it is a very important hearing and I commend the chairman for holding this hearing.

Senator LIEBERMAN. Thank you, Senator Baucus. Senator Grassley.

STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA

Senator GRASSLEY. Yes, Mr. Chairman, thank you for holding this hearing. It is a very necessary first step to getting the legislation passed.

I am sorry, too, that the Secretary of HUD could not be here but that should in no way detract from this Administration's commitments to Enterprise Zones because President Bush included in his State of the Union message to Congress, or his budget message in early February, his support for this legislation, and that was one of a large round of applause that he got.

It may have been because Jack Kemp was newly appointed to his Administration and because of Secretary Kemp's hard work on this. But without a doubt, this Administration is committed to the principle of Enterprise Zones and I think that we will get the support that we need.

I have not co-sponsored this legislation, but I surely support the concept and I want the Chairman and ranking minority member to know that I am going to work with them to help pass this legislation.

Also, Mr. Chairman, because I am going to be in and out this morning because of the debate on the floor, I would like to have permission, if I am not here, to submit some questions in writing to a couple of the panelists.

Senator LIEBERMAN. Yes, please do. Thank you, Senator Grassley. We will be glad to convey those to the panels.

[The prepared statement of Senator Wallop follows:]

STATEMENT BY SENATOR MALCOLM WALLOP
BEFORE THE SENATE COMMITTEE ON SMALL BUSINESS
REGARDING THE ENTERPRISE ZONE PROGRAM AND ITS IMPACT ON
SMALL BUSINESS GROWTH AND DEVELOPMENT
WEDNESDAY, JUNE 21, 1989

Thank you, Mr. Chairman, for calling today's hearing on the enterprise zone program and its potential impact on small business growth and development. I regret that Secretary Kemp could not be here to testify. As the main proponent of enterprise zones while a member of Congress, Secretary Kemp can provide some valuable insight as to how we here in Congress can encourage investment and stimulate the economy. While I would not argue that the key to enterprise zones is reducing the federal tax burden, I would also stress that enterprise zones are not necessarily an urban problem. As a rural state, Wyoming certainly has its share of economic development problems which could benefit from federal tax reductions.

I would note that there are currently two bills pending in Congress, H.R. 6, the Enterprise Zone Development and Employment Act of 1989 introduced by Congressman Rangel and S. 58, the Enterprise Zone Improvements Act of 1989, which was introduced by two members of this committee, Senators Boschwitz and Lieberman. Both of these bills would establisn tax incentives for businesses in enterprise zones. While I am certainly not opposed to using the Tax Code to encourage investments and economic development, I do have some reservations about adopting such limited tax incentives.

For example, I have long held the belief that a reduction in our capital gains tax would increase investments in small entrepreneurial companies. In fact, I have again cosponsored legislation to cut the capital gains tax and find it encouraging that Chairman Rostenkowski recently indicated that he might support such a reduction, if only temporarily. I, for one, believe it should be permanent, and I believe it will be. Under the existing tax structure, many small businesses have a difficult time finding one of the essential components to the success of their business -- that of equity capital. I believe a reduction in the capital gains tax would enhance their ability to obtain those investments, thus allowing them to expand their business, create new jobs and benefit a broader segment of our society.

Wyoming already has no personal or corporate income taxes, yet we still face some very tough economic development problems. We have a well-trained work force and an attractive living environment. So, I must question why the incentives offered for an enterprise zone would benefit my state and indeed our whole society more than a general tax reduction across the board. I would also venture to guess that there are other factors apart from tax incentives which play a major role in the ability of certain areas to attract new businesses.

In closing let me just say that I support the efforts of this Administration to revitalize urban and rural communities across the country. I look forward to hearing the testimony of the witnesses representing state enterprise zone programs. Perhaps they will share with us the positive aspects of their programs and give us their suggestions as to how we can craft a viable tax incentive proposal which will stimulate the growth of those neglected areas of the country. As we attempt to move ahead with such a proposal, I trust those suggestions will hold up to the test of the harsh realities of our budget deficit and the constraints of Gramm-Rudman.

Senator LIEBERMAN. Now, the first panel will be the people at the state level. Steve Heintz is the Commissioner of Economic Development for Connecticut, Louis Jambois, Director of Community Development, St. Paul, MN, accompanied by Tom Helgesen as Community Development Representative.

Gentlemen, I welcome you here and thank you for taking the time and making the effort to come. Obviously, our interest in hearing your testimony is to find out how enterprise legislation is working on the State level and how you view the legislation that Senator Boschwitz has introduced and I am proud to co-sponsor, that would add tax benefits to existing Federal legislation.

I would ask you to try to—as I believe the staff suggested—to try to limit your opening remarks to 5 minutes and that will allow all of us here to enter into a dialogue afterward. We have your testimony and we will include it for the record.

Commissioner Heintz is listed first on my list. Is that appropriate? I do not want you to think I am being parochial in calling him first. OK. It is a pleasure to welcome Commissioner Heintz here.

Actually, I have a certain amount of parochial pride here, because—well, I hate to admit that I am now this old. Steve Heintz was my Administrative Assistant when I became Senate Majority Leader in Connecticut in 1975 and in spite of that experience he has gone on to great things and is now a Commissioner of Economic Development.

STATEMENT OF STEPHEN B. HEINTZ, COMMISSIONER, DEPARTMENT OF ECONOMIC DEVELOPMENT, STATE OF CONNECTICUT

Mr. HEINTZ. Thank you very much, Senator and Members of the panel. It is really a very distinct pleasure for me to be here, both to talk about this significant issue and also to appear before Connecticut's new junior Senator who is a mentor of mine and somebody who has taught me so much over the years, and it is because of the experience that I had with you in large part that I have been able to go on and do the things that I do.

Senator BOSCHWITZ. First Abraham Lincoln and now this.

Mr. HEINTZ. I could go on my full 5 minutes about this, Senator, but I will restrict my remarks.

I also come to this issue with a very deep interest. As Senator Lieberman knows, I just completed 6 years as the State Welfare Commissioner in Connecticut concerned about the issues of poverty in a State of great wealth, where we have two of the Nation's 10 poorest cities, and now I am in the field of economic development, and one of my major interests is trying to bring together the two Connecticuts. The one wealthy and prosperous and working, and the other in the shadows of disadvantage and poverty.

So I think that the Enterprise Zone legislation before this Committee is one of the most important economic development and human development issues before the Congress this year.

I would like to tell you a little bit about the Connecticut experience with Enterprise Zones and then offer four points about the legislation being considered by this Committee.

I think that the Connecticut experience points out some of the great successes that States can achieve through aggressive and cre-

ative administration of Enterprise Zones, but our 6 years of experience has also taught us a few very important lessons, lessons that I think the Federal Government should consider as it crafts its own program.

Connecticut is currently riding the crest of an economic wave that has brought great prosperity to the vast majority of our people. We have had the Nation's highest per capita income for 3 years in a row. We have an unemployment rate that consistently hovers well below the national average, and our economic development climate earned one of the highest ratings Nationwide from the independent Corporation for Enterprise Development.

We are currently looking forward to the 1990's as a period of great challenge, but a period in which we think we can develop the kind of progressive strategies that will maintain our prosperity well into the future.

But this prosperity was hard-earned in Connecticut and I give much of the credit to Governor O'Neill and to the legislature for tackling some of the difficult issues of the early 1980s when Connecticut was in the throes of a serious economic contraction.

One of the key initiatives of those early years to try to bring prosperity to a troubled state was the Enterprise Zone program. Connecticut became the first state in the Nation to establish Enterprise Zones when the Governor signed enabling legislation in July 1981.

The first six zones in Connecticut opened for business the following October, ranging in size from 125 to 700 acres. The program proved so successful that four new zones were created in 1986, bringing the statewide total to 10.

Connecticut is a small State, but the numbers speak for themselves. There are 1,284 projects statewide in our zones, representing a total investment by the private sector of some $375 million. More than 6,600 jobs have been created and Enterprise Zone benefits have helped retain an additional 6,900 jobs.

As delighted, of course, as we are, with the benefits the Enterprise Zones have brought to our cities, I am convinced that more can be done and should be done. The legislation introduced by Senator Boschwitz and co-sponsored by Senator Lieberman would be a major step in the right direction and I applaud the sponsors for their commitment to this very important program.

As we have found in Connecticut, tax incentives can make the difference in an individual firm's decision to invest in an Enterprise Zone versus another location. To the extent that Federal Enterprise Zones overlap with zones designated by the States, the States could offer a very potent combination of Federal and State property and income tax incentives.

But as this legislation moves forward I would like to call your attention to four issues and offer four suggestions that I think might make Enterprise Zones an even more attractive a location for business investment.

The first has to do with ensuring that the benefits of Enterprise Zones extend to the residents who live in them. For example, title 2 of the bill offers credits to employers for hiring disadvantaged people as employees, and in principle of course this is unarguably good.

But in practice, we have found that companies have not taken advantage of this type of benefit as much a we would like. The reason is because many of the residents of the zones lack the sufficient basic education and basic skills to fill the jobs that the companies are creating.

So for this reason, I believe that it is important that you consider adding to the bill some form of tax credit for those companies who invest in the education and training of new employees who are residents from that zone. The companies are going to have to invest in that kind of activity if in fact the residents of these blighted urban neighborhoods are going to be able to fill the new jobs being created.

As the Federal Government moves to establish zones, a high priority should be given to extending Federal benefits uniformly around the areas in which States have already established their own zone.

My nightmare is that a Federal zone might include part of a State zone but not all of it. That is creating one area in a zone where the benefits would be greater than in the next and I think providing a part of a zone that might be more attractive than another, undermining our efforts to develop the entire zone and complicating the administration of the State program.

So a possible remedy for this issue would be to include a provision in the legislation that extends the Federal Enterprise Zone benefits to an entire State zone, if the Federal zone includes any part of a previously designated State Enterprise Zone.

A third issue is ease of administration. If there is one consistent criticism of our own program in Connecticut, it is the complexities of administration in dealing with the requirements of compliance, and ideally Federal and State zones should form a true partnership. Property and business tax benefits at the State level can combine with capital gains and income tax benefits at the Federal level to create a real economic development synergy.

But consider the perspective of a potential tenant in an Enterprise Zone. It would be far easier for this company to consult with only one agency to learn about the benefits of investing in that zone. Having to work with administrators from both the Federal and State levels only complicates the paperwork and could create a disincentive to Enterprise Zone investment.

So I would suggest that the Senate consider adding language that would encourage HUD to contract with State Enterprise Zone agencies to administer the Federal program. If implemented, this could create one-stop shopping for any company that was considering an Enterprise Zone location and streamline the administration of the program.

A final concern has to do with the process by which HUD will designate the Federal Enterprise Zones. Under current law, as you know, Secretary Kemp is authorized to select up to 100 Enterprise Zones nationwide based upon fairly rigid guidelines incorporating demographic data of indicators of economic distress.

But this selection process does not take into account the degree of community support for an Enterprise Zone. In Connecticut, as you will hear from our panel later on this morning, we have found that our most successful zones have emerged from those communi-

ties in which public and private sector support for the zone has been the strongest.

If the Congress wishes to achieve the greatest possible return on its multi-billion-dollar investment, I believe HUD's selection criteria should capture and rank in order of priority the level of community support and private sector support for an Enterprise Zone and I would encourage you to specify that kind of analysis as the Secretary is making his determination.

I want to thank you again for this opportunity to present these brief comments this morning. I would be very eager to work with the Members of this Committee over the weeks and months ahead on this legislation and I would be happy to answer any questions that you may have.

Thank you very much.

[Material follows:]

STATE OF CONNECTICUT
DEPARTMENT OF ECONOMIC DEVELOPMENT

STEPHEN B. HEINTZ
Commissioner

July 28, 1989

The Hon. Joseph Lieberman
The Hon. Rudy Boschwitz
United States Senate
Committee on Small Business
Washington, D.C. 20510-6350

Dear Senator Lieberman and Senator Boschwitz:

Thank you very much for your letter of June 26, and for the opportunity to testify before you about the proposed federal enterprise zone program. The committee meeting was both fascinating and informative, and I hope to have many more opportunities to appear before you in the future.

Connecticut led the nation in establishing enterprise zones in 1982, offering a wide range of state and local incentives, as well as administrative support, to help develop distressed urban areas. Our experience has shown that tangible incentives can lead to positive results -- nearly $400 million in new investment and the creation or retention of more than 13,000 jobs in six years. I feel this knowledge base gives us unique insights into the proposed federal enterprise zones.

With this in mind, it gives me great pleasure to reply to Senator Grassley's questions.

1. The point can be made that businesses from right outside the federal enterprise zone boundary could relocate inside the zone. This could have the effect of weakening the outside area without benefiting the entire region. Do you agree with this point, and if so would you support adding a provision to the federal program preventing a business from abandoning a facility solely to relocate within a federal enterprise zone?

A. In theory, a business could decide to "cross the street" in order to take advantage of enterprise zone benefits. In practice, we have found this not to be the case. Location and relocation decisions are usually made for reasons far more significant to a business than tax benefits: product markets, labor availability or costs, transportation needs, physical space requirements, and the like.

The availability of tax benefits in one area may serve to make it more attractive for investment than another, but only after more important criteria have been satisfied. I would therefore not support a provision barring enterprise zone benefits to a company that was interested in making an investment in the zone. On the margin, it would only serve to discourage investment in precisely the area in which investment should be encouraged.

2. The point will also be made that businesses could leave the federal enterprise zone without penalty after a few years of drawing down the enterprise zone benefits. Would you support instituting penalties if a business withdraws from an enterprise zone soon after the benefits have expired?

A. No. Inasmuch as "tax shopping" plays a minor role in a business location decision, tax penalties could only serve to drive away firms that are considering an enterprise zone investment.

3. A recent study done by Professor Dennis Grady, formerly of the University of Northern Iowa, entitled "The Second War Over the States," concluded that tax credits have absolutely no influence on business location. Professor Grady also concluded that the labor force is one of the most important factors, including the education of the population. Could you comment on these findings?

A. I disagree with the conclusion that tax benefits have no influence over business location decisions. As a marketing tool, they are highly effective in drawing corporate attention to a particular community or neighborhood. Once a business is interested in an enterprise zone site, we can then talk about a package of incentives -- of which tax credits are but one part -- that can ultimately lead to a decision to locate, relocate or expand in the enterprise zone.

Professor Grady's point about the labor force is well taken. One of the reasons Connecticut has been so successful in attracting new businesses over the years is our highly educated and extremely productive labor pool. The independent Corporation for Enterprise Development, in its annual review of the economic development climate in the 50 states, cited our educated work force as one of the most attractive aspects of a Connecticut location.

Thank you again for this opportunity to comment on the federal enterprise zone program. Please do not hesitate to contact me if I can be of any further assistance.

Best regards,

Stephen B. Heintz
Commissioner

Senator LIEBERMAN. Thank you.

Senator BOSCHWITZ. I welcome this morning two Minnesotans. As I told the Senator from Connecticut I do not really know them very well and I am not sure that I have met Mr. Helgesen before.

Mr. Jambois is the Director of Community Development, Department of Trade and Economic Development for the State of Minnesota. We welcome you here and look forward to your testimony. We will get a good sense of how enterprise zones work in Minnesota in relationship to what we have just heard from Connecticut.

Please proceed, whichever one of you is going to give the testimony.

STATEMENT OF LOUIS JAMBOIS, DIRECTOR OF COMMUNITY DEVELOPMENT, MINNESOTA DEPARTMENT OF TRADE AND ECONOMIC DEVELOPMENT, ACCOMPANIED BY TOM HELGESEN, COMMUNITY DEVELOPMENT REPRESENTATIVE

Mr. JAMBOIS. Thank you, Mr. Chairman. In the interest of time I will present the testimony for both Tom and myself and we will both then stand to take questions later.

The Minnesota Enterprise Zone Program began in 1983 and provided for two types of zones. The first was the border-cities zone program which was located on our western border. The cities needed a program to help retain businesses which were subject to very aggressive recruitment campaigns from the Dakotas.

The Minnesota businesses paid higher property taxes and worker compensation insurance rates and the border-city program permitted these cities to grant State tax credits and local tax reductions to the businesses to reduce the fiscal disparities between the States.

In 1 year before the program started, one of our border cities had 40 to 50 businesses leave the community. In 6 years since the program started, less than 25 businesses have left.

We can conclude, then, from this type of program that Enterprise Zones can stabilize a business community, allowing its businesses to stay and prosper in an area instead of leaving and can prevent a distressed area from further economic slide and lay a foundation for future restoration.

A second type of Minnesota zone is called a competitive zone, and this is a more traditional type of zone that we have heard about from Connecticut.

To get a competitive zone designation communities have to first define an economic hardship area within which a zone would be located. The hardship areas must meet both a distress and a population criteria. The zone can be located anywhere within the hardship area subject to acreage and value limitations.

In Minnesota we permit noncontiguous, or scattered site zones, and in some cases we actually permit the grouping of small rural communities into a single zone.

After meeting economic distress and physical characteristic criteria, a community's request for designation has to be evaluated by additional criteria, including the local commitment of resources and a local development and tax credit use plan. Under the Minnesota program, six border city zones have been created and 10 com-

petitive zones have been created, but the competitive zones include 19 cities in those 10 zones.

We have four types of tax credits, as Senator Boschwitz has implied. We have a State-paid tax credit for newer, expanding facilities. We have an income tax credit for the cost of interest on construction financing, we have an income tax credit of up to $3,000 for a new job created, and we have a general sales tax credit for construction materials or equipment.

Now, Minnesota has a cap on the amount of tax credits that can be used in both the overall program and by each zone. Tax credits of $39 million have been allocated for the entire program and each zone has a predetermined share of this allocation.

Subject to State approval, a local EZ coordinator can negotiate the type and amount of tax credits to go to each business for a particular project within the zone. The credits can be drawn down to over a 5-year period.

If the amount of the credits exceeds the tax liability for 1 year the business actually receives a refund. This refundable feature is a particular help to new businesses that may not have a tax liability in their start-up phase. By contrast, the Federal program does not provide for refunds for either employers or employees.

The Minnesota program relies very heavily on local government involvement and local contribution, but it is not a staff-intensive program. Most local coordinators spend less than one-tenth time on this program annually and our State coordinator, Tom Helgesen, spends one-third to one-half time on the Enterprise Zone Program, yet between 600 and 800 businesses receive these credits each year. So we get a lot of bang for our dollar.

Since 198 v3 the program has resulted in the creation of over 5,200 new jobs and the retention of 6,000 to 8,000 jobs annually for about $2,300 per job spread over 5 years. The $2,300 is spread over a 5-year period of time and of course because this is a tax credit program, all claims are subject to tax audit and I think this is an important safeguard for fraud prevention.

Based on our understanding of S. 58 and H.R. 6 and our experience, we would like to very respectfully suggest some changes in the program being proposed by the Federal Government.

No. 1, we recommend that the program include additional designation factors besides rank order of distress, including a sound local financial commitment and a local development and use plan and finally, targeting the program to disadvantaged people in the target area. I think this coincides very nicely with the testimony you heard from Connecticut.

No. 2, we recommend that the zones be configured in whatever way best links the distressed population with developable, or redevelopable commercial and industrial property. If developable land lies adjacent to a census tract with a distressed population, it should be included in a proposed zone without fear that it would weaken an applicant's distress criteria, or distress ranking.

Currently, No. 3, businesses from just outside the Federal zone boundaries could relocate inside a zone and collect credits. While we think this would strengthen the zone, we think it would weaken the adjacent areas. In Minnesota we prevent this practice and we

recommend that a provision be added to the Federal program which also prevents the practice.

No. 4, as currently proposed, businesses could leave the Federal Enterprise Zone without a penalty after a few years of drawing down the credits, which are very, very generous on the front end of the program. Again, we prevent this practice in the State of Minnesota by requiring refunds of credits if a business ceases to operate or significantly scales back its activity in a zone and we suggest that you also review that policy.

No. 5, as currently proposed businesses could use tax benefits to assist a company to move from one city to another. Again, we try to prevent this in Minnesota and we recommend that you also attempt to prevent this practice. We think it is also consistent with other programs such as community development block grants and UDAG grants.

S. 58 provides job credits—this is No. 6—for new wages paid in a zone and can run in excess of 20 years. By our calculations, this could result in a tax expenditure of thousands and thousands of dollars for each job created. We believe this far exceeds the dollars per job of other Federal programs and is not warranted.

We would recommend that the job creation benefits be reduced to a maximum of 7 to 10 years and that a cap on yearly tax credit be established at about $2,000 to $3,000. Our experience suggests that these amounts and benefit periods would be more than adequate incentive for job creation.

No. 7, the current program does not set a cap on total cost. Our experience suggests that it is possible to cap job creation credits and zone credits without crippling the program and without creating a huge bureaucracy to administer it. Caps will make the EZ Program more accountable and cost-effective.

After the Government gains experience with the program it can then decide whether the benefits are enough to accomplish the program's goals, decide if the program pays for itself, and if the caps should be raised or lowered.

Finally, we encourage the Committee to give serious consideration to rural Enterprise Zones. Rural designations of 33 are too few, and we believe that the designations could be substantially increased and that cooperating rural communities should be allowed to apply as one proposed zone.

At this point I would like to thank the Committee for inviting Tom and myself to the hearing today. I want to reaffirm Minnesota's support for a Federal program and pledge our assistance should you request it. Of course, we stand ready to respond to any questions that you may have.

Thank you very much.

[The prepared statement of Mr. Jambois follows:]

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TESTIMONY OF LOUIS JAMBOIS
AND TOM HELGESEN
STATE OF MINNESOTA TO THE
U.S. SENATE SMALL BUSINESS COMMITTEE
WEDNESDAY, JUNE 21, 1989

I. HISTORY OF THE MINNESOTA ENTERPRIZE ZONE PROGRAM

THE MINNESOTA ENTERPRISE ZONE PROGRAM BEGAN IN 1983 AND PROVIDED FOR TWO TYPES OF ZONES (EZ's). THE FIRST WAS "BORDER-CITY ZONES" FOR CITIES LOCATED ON OUR BORDER WITH THE DAKOTAS. THESE CITIES NEEDED A PROGRAM TO HELP RETAIN THEIR BUSINESSES WHICH WERE SUBJECT TO AGGRESSIVE RECRUITMENT CAMPAIGNS FROM THE DAKOTAS. MINNESOTA BUSINESSES PAID HIGHER PROPERTY TAXES AND WORKER'S COMPENSATION INSURANCE PREMIUMS THAN BUSINESSES IN THE DAKOTAS, PARTICULARLY IN NORTH DAKOTA. THE BORDER CITY EZ PROGRAM PERMITS THESE CITIES TO GRANT STATE TAX CREDITS AND LOCAL TAX REDUCTIONS TO BUSINESSES THROUGHOUT THE CITIES TO REDUCE PROPERTY TAXES AND PARTIALLY COMPENSATE BUSINESSES FOR THE HIGHER WORKERS' COMPENSATION COSTS. THIS HAS HELPED THE BORDER CITIES TO REDUCE THE FISCAL DISPARITIES BETWEEN THE STATES AND THEREBY STABILIZE THEIR LOCAL BUSINESS COMMUNITIES AND PREVENT BUSINESS FLIGHT ACROSS THE BORDER. IN ONE YEAR BEFORE OUR PROGRAM STARTED ONE OF OUR BORDER CITIES (MOORHEAD - POP. 30,000) SAW BETWEEN 40 AND 50 BUSINESSES LEAVE THE COMMUNITY. IN THE SIX YEARS SINCE THE PROGRAM STARTED, THE TOTAL IS UNDER 25 FOR ALL YEARS COMBINED - REPRESENTING A MORE NORMAL BUSINESS INFLOW AND OUTFLOW. THE SUCCESS OF OUR BORDER CITY PROGRAM IN RETAINING BUSINESSES AND JOBS ILLUSTRATES ONE VERY IMPORTANT USE OF EZ's OTHER THAN CREATING JOBS AND NEW INVESTMENT: EZ's CAN STABILIZE A BUSINESS COMMUNITY ALLOWING ITS BUSINESSES TO STAY AND PROSPER INSTEAD OF LEAVING; THIS CAN PREVENT A DISTRESSED AREA FROM SLIDING FURTHER DOWNHILL AND PROVIDE A FOUNDATION TO RESTORE THE AREA.

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THE SECOND TYPE OF MINNESOTA EZ IS CALLED A "COMPETITIVE ZONE." THIS IS A MORE TRADITIONAL TYPE OF EZ. TO GET A COMPETITIVE EZ DESIGNATION, COMMUNITIES HAD TO FIRST DEFINE AN ECONOMIC HARDSHIP AREA WITHIN WHICH THE EZ WOULD BE LOCATED. THE HARDSHIP AREAS HAD TO MEET AT LEAST TWO OF SIX MEASURES OF DISTRESS AND CONTAIN MINIMUM POPULATIONS OF 4,000 FOR URBAN OR 2,500 FOR RURAL AREAS. THE EZ ITSELF COULD BE LOCATED ANYWHERE WITHIN THE HARDSHIP AREA AS LONG AS THE EZ CONTAINED NO MORE THAN 400 ACRES AND HAD TAXABLE PROPERTY WITH A MARKET VALUE PER ACRE OF NO MORE THAN $100,000 RURAL OR $300,000 URBAN. WHILE THE ZONE ITSELF HAD NO MINIMUM POPULATION REQUIREMENT, ITS BOUNDARIES HAD TO BE CONTINUOUS AND INCLUDE VACANT OR UNDERUTILIZED PROPERTY. (NOTE: ONE OF OUR MOST SUCCESSFUL ZONES IN THIEF RIVER FALLS, HAS NO RESIDENTIAL POPULATION, IS ENTIRELY INDUSTRIAL AND HAS CREATED ALMOST 600 NEW JOBS FOR THE ADJACENT POPULATION OF 9,000 PEOPLE FOR A COST OF ABOUT $1.5 MILLION IN STATE TAX CREDITS.) IN MINNESOTA WE PERMIT DISCONTINUOUS PARCELS TO BE MADE CONTINUOUS BY A CONNECTING LINE-IN EFFECT PERMITTING SCATTERED-SITE ZONES AND IN SOME CASES PERMITTING A CLUSTERING OF SMALL RURAL CITIES INTO ONE ZONE.

AFTER MEETING THE ABOVE ECONOMIC DISTRESS CRITERIA AND PHYSICAL CHARACTERISTICS ELIGIBILITY CRITERIA, A COMMUNITY'S REQUEST FOR DESIGNATION HAD TO BE EVALUATED BY COMPETITIVE CRITERIA INCLUDING AMONG OTHERS, THE FOLLOWING: PERVASIVENESS OF DISTRESS; EXTENT OF PROPERTY ABANDONMENT; DETERIORATION AND TAX ARREARAGES; THE PROSPECTS FOR NEW INVESTMENT AND ECONOMIC DEVELOPMENT; A COMMUNITY'S PROPOSED USE OF OTHER PROGRAMS TO INCREASE THE PROBABILITY OF NEW INVESTMENT; THE EXTENT TO WHICH PROJECTED DEVELOPMENT WOULD PROVIDE EMPLOYMENT TO DISADVANTAGED AND UNEMPLOYED RESIDENTS OF THE HARDSHIP AREA.

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COMMUNITIES ALSO HAD TO PROVIDE WITH THEIR APPLICATIONS, A DEVELOPMENT PLAN OUTLINING THE TYPES OF INVESTMENT AND DEVELOPMENT THAT WOULD RESULT FROM EZ DESIGNATION, PROJECTED JOB CREATION NUMBERS, WAGE LEVELS AND TARGETING AS WELL AS A COMMITMENT TO PROVIDE A LOCAL CONTRIBUTION AND A PLAN FOR HOW THEY PROPOSED TO USE STATE TAX CREDITS TO ACCOMPLISH THEIR INVESTMENT AND DEVELOPMENT GOALS.

UNDER THE MINNESOTA PROGRAM, SIX CITIES WERE DESIGNATED AS BORDER CITY ZONES AND 19 CITIES HAD AREAS INCLUDED IN 10 COMPETITIVE ZONES. IN ADDITION, EACH BORDER CITY IDENTIFIED ITS OWN TARGET AREAS THAT FUNCTIONED LIKE THE COMPETITIVE ZONES.

II. HOW THE MINNESOTA PROGRAM WORKS

SUBJECT TO STATE LAW AND WITHIN THE GUIDELINES OF THEIR OWN LOCAL PLANS, COMPETITIVE ENTERPRISE ZONES (INCLUDING BORDER CITY TARGET AREAS) CAN WORK WITH THEIR BUSINESSES AND PROSPECTIVE BUSINESSES TO PROVIDE FOUR TYPES OF TAX CREDITS OR REDUCTIONS:

1. A STATE-PAID PROPERTY TAX CREDIT APPLIED TO NEW OR EXPANDED FACILITIES IN THE ZONE.

2. AN INCOME TAX CREDIT FOR A PORTION OF THE COST OF INTEREST TO FINANCE EZ CONSTRUCTION.

3. AN INCOME TAX CREDIT OF UP TO $3,000 ANNUALLY TO AN EMPLOYER FOR EACH ADDITIONAL WORKER EMPLOYED IN THE ZONE (EXCLUDING CONSTRUCTION WORKERS).

4. EXEMPTION FROM THE GENERAL SALES TAX FOR PURCHASING CONSTRUCTION MATERIALS OR EQUIPMENT FOR USE IN THE ZONE. THE TAX IS FULLY PAID AND REIMBURSED AS AN INCOME TAX CREDIT.

THE MINNESOTA PROGRAM HAS SEVERAL UNUSUAL OR UNIQUE FEATURES. ONE OF THESE IS A LEGISLATIVE CAP ON THE AMOUNT OF TAX CREDITS THAT CAN BE USED IN THE OVERALL PROGRAM AND BY EACH ZONE. THE LEGISLATURE HAS ALLOCATED $39,000,000 IN TAX CREDITS FOR THE ENTIRE PROGRAM STATEWIDE. EACH ZONE HAS ITS OWN SHARE OF THIS ALLOCATION THAT IT IS BOUND BY CONTRACT AND LAW NOT TO EXCEED. EACH ZONE HAS A LOCAL COORDINATOR WHO NEGOTIATES PROSPECTIVE PROJECTS WITH NEW OR EXISTING BUSINESSES. USING STATE AND LOCAL GUIDELINES, AN EZ CITY WILL APPROVE THE TYPE AND AMOUNT OF TAX CREDITS TO GO TO A BUSINESS FOR A PARTICULAR PROJECT WITHIN THE ZONE. THIS IS SUBJECT TO STATE APPROVAL. THE CREDITS CAN BE DRAWN DOWN OVER A PERIOD NOT TO EXCEED FIVE YEARS. EACH YEAR THE BUSINESS WILL MEET WITH THE ZONE COORDINATOR, SHOW EVIDENCE OF WHAT HAS BEEN ACCOMPLISHED TO EARN THE CREDITS FOR THAT YEAR AND FILL OUT A ONE PAGE FORM AUTHORIZING THE TAX CREDIT DRAWDOWN. THE FORM IS REVIEWED AND APPROVED BY THE CITY AND STATE (COMMISSIONER OF TRADE AND ECONOMIC DEVELOPMENT) AND AN ORIGINAL SIGNED COPY IS FILED WITH THE INDIVIDUAL OR CORPORATE INCOME TAXES TO RECEIVE THE DRAWDOWN. IF THE AMOUNT OF CREDITS EXCEEDS THE TAX LIABILITY FOR THAT YEAR, THE BUSINESS RECEIVES A REFUND. THIS "REFUNDABLE" FEATURE OF THE MINNESOTA PROGRAM IS OF PARTICULAR HELP TO NEW BUSINESSES THAT MAY NOT HAVE A TAX LIABILITY IN THEIR START-UP PHASE. (THE PROPOSED FEDERAL PROGRAM BY CONTRAST, ONLY ALLOWS A CARRY FORWARD AND BACKWARDS OF CREDITS THAT EXCEED TAX LIABILITY; IT TRIES TO PROVIDE FOR CASH NEEDS IN OTHER WAYS.)

THE MINNESOTA PROGRAM THEN, RELIES HEAVILY ON LOCAL GOVERNMENT INVOLVEMENT BY REQUIRING A THOUGHTFUL LOCAL DEVELOPMENT PLAN, A TIE-IN OF EZ CREDITS WITH OTHER RESOURCES AND LOCAL CONTRIBUTION, TARGETING THE IMPACT TO BOTH PLACES (ZONES) AND PEOPLE (HARDSHIP AREAS), NEGOTIATING THE AMOUNT AND TYPE OF CREDITS FOR EACH BUSINESS PROJECT, AND CHECKING PROGRESS EACH YEAR. SURPRISINGLY, THE PROGRAM IS NOT VERY STAFF INTENSIVE. THE LARGEST ZONE, MOORHEAD (400-500 BUSINESSES PER YEAR AND $1-1.5 MILLION PER YEAR IN STATE TAX CREDITS) USES ONE PROFESSIONAL AND ONE CLERICAL PERSON 1/3 OF FULL-TIME EACH; MOST LOCAL COORDINATORS SPEND MUCH LESS THAN ONE-TENTH TIME ANNUALLY. THE STATE ADMINISTRATOR SPENDS 1/3-1/2 TIME ON THE STATE ADMINISTRATION OF THE PROGRAM (600-800 BUSINESSES AND $4-8 MILLION PER YEAR).

III MINNESOTA ENTERPRISE ZONE PROGRAM ACCOMPLISHMENTS.

WHEN WE ADD OUR PRELIMINARY DATA FOR 1988 TO THE CUMULATIVE DATA REPORTED IN THE 1987 ANNUAL REPORT (WHICH HAS BEEN HANDED OUT TO YOU) WE FIND THAT OUR PROGRAM HAS RESULTED IN THE CREATION OF 5,221 NEW JOBS, THE RETENTION OF 6-8,000 JOBS ANNUALLY (MOSTLY IN BORDER CITY ZONES) FOR AN EXPENDITURE OF $28,000,000 IN STATE TAX CREDITS.

THESE FIGURES ARE PROVIDED TO THE STATE ANNUALLY BY LOCAL COORDINATORS WHO, AS MENTIONED EARLIER, MONITOR BUSINESS PERFORMANCE INDIVIDUALLY EACH YEAR. WE HAVE NOT COLLECTED FIGURES ON THE LEVEL OF BUSINESS INVESTMENT DOLLARS STIMULATED BY THE PROGRAM.

MINNESOTA RECOMMENDATIONS

BASED UPON OUR UNDERSTANDING OF THE TITLE VII PROCESS AND THE LEGISLATION AND ISSUES UNDER CONSIDERATION AND OUR EXPERIENCE, WE WOULD LIKE TO MAKE RECOMMENDATIONS TO THE U.S. SENATE SMALL BUSINESS COMMITTEE REGARDING POSSIBLE CHANGES IN THE FEDERAL ENTERPRISE ZONE (F.E.Z.) PROGRAM.

RECOMMENDATIONS

FIRST, I WOULD LIKE TO STRESS TO THE COMMITTEE THAT WE THINK THE MOST IMPORTANT CONSIDERATION WITH ALL OF THE PROPOSED LEGISLATION IS THAT CONGRESS ACT SOON TO ENACT AN ENTERPRISE ZONE LAW THAT PUTS REAL BENEFITS INTO THE FEDERAL PROGRAM AND GETS THE DESIGNATION PROCESS MOVING ALONG TO FRUITION. WHILE WE HAVE SUGGESTIONS FOR CHANGES, WE BELIEVE THE 1989 ENTERPRISE ZONE IMPROVEMENTS ACT AND RURAL ENTERPRISE ZONE ACT, WITH A FEW CHANGES, ARE BASICALLY SOUND PIECES OF LEGISLATION THAT WILL RESULT IN SUCCESSFUL, BENEFICIAL ZONES.

THERE ARE OVER 270 COMMUNITIES THROUGHOUT THE COUNTRY WHO HAVE INVESTED SUBSTANTIAL TIME AND EFFORT TO PROPOSE ENTERPRISE ZONES FOR DESIGNATION AND DESERVE THE COOPERATION OF CONGRESS IN MOVING THE PROCESS ALONG AND GIVING THE PROGRAM FINANCIAL SUBSTANCE.

OUR RECOMMENTATIONS FOLLOW:

I. FEZ DESIGNATIONS AND APPLICATIONS:

A. WE RECOMMEND THAT THE HCD TITLE VII PROCESS BE CHANGED TO INCLUDE ADDITIONAL DESIGNATION FACTORS BESIDES RANK ORDER OF DISTRESS. IN MINNESOTA, ADDITIONAL FACTORS INCLUDED THE FOLLOWING:

1. LOCAL COMMITMENT AND MATCHING RESOURCES;
2. A LOCAL DEVELOPMENT PLAN THAT INCLUDED INVESTMENT AND JOB CREATION PROSPECTS AND STRATEGIES; AND
3. TARGETING THE IMPACT TO DISADVANTAGED RESIDENTS.

WE ENCOURAGE THE COMMITTEE TO CONSIDER ADDING SOME OR ALL OF THESE FACTORS AS CRITERIA FOR DESIGNATION RANKING.

B. WE RECOMMEND THAT IF THE APPLICATION PROCESS IS RE-OPENED, APPLICANTS BE ALLOWED TO STRUCTURE THEIR PROPOSED ZONES SO THAT THE PHYSICAL CHARACTERISTICS OF THE ZONE (WHERE THE PHYSICAL IMPROVEMENTS TAKE PLACE) CAN BE TREATED SOMEWHAT DIFFERENTLY FROM THE AREA WHERE THE DISTRESSED POPULATION LIVES.

IN MINNESOTA, OUR APPLICANTS FIRST CHOSE A RELATIVELY COMPREHENSIVE GEOGRAPHIC AREA THAT INCLUDED THE POPULATION AND INFRASTRUCTURE THAT MET THE ELIGIBILITY MEASURES OF DISTRESS. THIS WAS THE AREA OF IMPACT OR "HARDSHIP AREA." THEN THE SMALLER ENTERPRISE ZONE ITSELF, ALTHOUGH IT HAD TO BE WITHIN THE HARDSHIP AREA AND WAS SUBJECT TO ACREAGE LIMITS, COULD BE CONFIGURED IN WHATEVER WAY BEST LINKED THE DISTRESSED POPULATION WITH DEVELOPABLE (OR RE-DEVELOPABLE) COMMERCIAL/INDUSTRIAL PROPERTY. THIS ALLOWED THE EZ TO SERVE BOTH PLACES AND PEOPLE. THEREFORE, IF GOOD DEVELOPABLE LAND LIED ADJACENT TO A CENSUS TRACT WITH DISTRESSED POPULATION, IT COULD BE INCLUDED IN A PROPOSED ZONE WITHOUT FEAR THAT IT WOULD WEAKEN AN APPLICANT'S DESIGNATION RANKING.

THE FEDERAL PROGRAM, AS CURRENTLY PROPOSED, DOES NOT ALLOW THIS FLEXIBILITY. WE RECOMMEND THAT ZONE PROPOSALS FOR THE FEDERAL PROGRAM BE GIVEN THE SAME FLEXIBILITY.

II. FEATURES AND CHARACTERISTICS OF PROPOSED FEDERAL LEGISLATION THAT CAN ADDRESS ENTERPRISE ZONE PROBLEMS.

A. PROBLEM - BUSINESSES FROM JUST OUTSIDE THE FEZ BOUNDARIES COULD RELOCATE INSIDE THE ZONE. THIS WOULD STRENGTHEN THE ZONE WHILE WEAKENING THE ADJACENT AREA WITHOUT BRINGING ANY NEW BENEFIT TO THE ENTIRE AREA OR MUNICIPALITY.

DISCUSSION - IN MINNESOTA BEFORE A BUSINESS PROJECT IS APPROVED FOR EZ TAX CREDITS, THE LOCAL GOVERNMENT MUST MAKE A FINDING THAT THE EZ PROJECT "WILL NOT RESULT IN THE REDUCTION OF THE ASSESSED VALUE OF EXISTING PROPERTY WITHIN THE MUNICIPALITY OWNED BY THE APPLICANT, THROUGH ABANDONMENT, DEMOLITION, OR OTHERWISE, WITHOUT PROVISION FOR THE RESTORATION OF THE EXISTING PROPERTY WITHIN A REASONABLE TIME IN A MANNER SUFFICIENT TO RESTORE THE ASSESSED VALUATION." THIS PREVENTS BUSINESSES FROM ABANDONING PROPERTY IN A CITY TO MOVE INTO THE ZONE.

SOLUTION: WE RECOMMEND THAT A PROVISION BE ADDED TO THE FEDERAL PROGRAM PREVENTING A BUSINESS FROM ABANDONING A FACILITY SOLELY TO RELOCATE WITHIN A FEZ.

B. PROBLEM - AS CURRENTLY PROPOSED, BUSINESSES COULD LEAVE THE FEZ WITHOUT PENALTY AFTER A FEW YEARS OF DRAWING DOWN THE FEZ BENEFITS WHICH ARE HEAVILY LOADED ON THE FRONT END.

DISCUSSION - IN ADDITION TO THE ONGOING YEAR-AFTER-YEAR BENEFITS A BUSINESS CAN GET IN A FEZ, THERE ARE CERTAIN FRONT-END BENEFITS THAT ARE SUBSTANTIAL:

- 10% INVESTMENT TAX CREDIT FOR EZ CONSTRUCTION.
- "EQUITY EXPENSING" (OR INCOME TAX DEDUCTABILITY) OF THE PURCHASE OF EZ STOCK UP TO $100,000.
- 50% TAX CREDIT ON WAGES OF DISADVANTAGED WORKERS, PHASING DOWN TO 10% IN YEAR 7.
- INDUSTRIAL DEVELOPMENT BONDS MIGHT BE USED.
- ACCELERATED COST RECOVERY METHOD OF DEPRECIATION.
- POSSIBLE USE OF SPECIAL REVOLVING LOAN FUNDS CARRYING FAVORABLE TERMS.

AFTER 3-7 YEARS OF DRAWING THESE BENEFITS, A BUSINESS COULD LEAVE THE ZONE WITH LITTLE OR NO PENALTY. IN MINNESOTA WE HAVE A PROVISION TO PREVENT THIS CALLED RECAPTURE - IF A BUSINESS CEASES TO OPERATE IN AN ENTERPRISE ZONE WITHIN 2 YEARS AFTER THE EXPIRATION OF TAX BENEFITS, THE TAX BENEFITS IT HAS RECEIVED ARE SUBJECT TO RECAPTURE. (THERE IS A SLIDING SCALE FROM 0-2 YEARS SO THAT BY 2 YEARS AFTER RECEIVING BENEFITS NO REPAYMENT OR RECAPTURE IS NECESSARY.)

SOLUTION - ADD A PROVISION TO THE FEDERAL ENTERPRISE ZONE PROGRAM REQUIRING PARTIAL OR FULL REPAYMENT OF BENEFITS RECEIVED IF A BUSINESS LEAVES OR SIGNIFICANTLY SCALES BACK ITS OPERATIONS IN A ZONE WITHIN A PERIOD OF TIME AFTER RECEIVING BENEFITS.

C. PROBLEM: AS CURRENTLY PROPOSED BUSINESSES COULD USE FEZ TAX BENEFITS TO ASSIST A MOVE FROM ONE MUNICIPALITY TO ANOTHER.

DISCUSSION: IN MINNESOTA WE HAVE AN ANTI-PIRATING PROVISION THAT PREVENTS THE USE OF EZ TAX BENEFITS WHEN IT WOULD HAVE THE EFFECT OF TRANSFERRING EMPLOYMENT FROM ONE MUNICIPALITY TO ANOTHER.

SOLUTION: ADD A PROVISION TO THE FEZ PROGRAM TO PREVENT THE USE OF FEZ BENEFITS TO TRANSFER EMPLOYMENT FROM ONE MUNICIPALITY TO ANOTHER.

D. PROBLEM: JOB CREATION TAX CREDITS FOR NEW WAGES PAID IN A FEZ CAN RUN IN EXCESS OF 20 YEARS IN MANY CASES. AT A RATE OF 10% PER YEAR, THIS COULD RESULT IN A TAX EXPENDITURE OF MORE THAN 2 YEARS' OF WAGES PER JOB. EVEN A MODESTLY PAYING JOB OF $15,000 PER YEAR WOULD RESULT IN A TAX EXPENDITURE OF OVER $30,000 FOR ONE JOB CREATION. THIS FAR EXCEEDS THE DOLLARS PER JOB CREATION CRITERIA OF OTHER FEDERAL PROGRAMS.

DISCUSSION: IN MINNESOTA WE ALLOW A MAXIMUM OF $3,000 IN TAX CREDITS PER NEW JOB PER YEAR. IT IS ALMOST ALWAYS GRANTED FOR JUST ONE YEAR. THE MAXIMUM NUMBER OF YEARS IS FIVE. THEREFORE, THE MAXIMUM THAT COULD BE DRAWN DOWN FOR ANY NEW JOB IS $15,000. IRRESPECTIVE OF OTHER EZ BENEFITS, OUR JOB CREATION TAX EXPENDITURES RUN LESS THAN $3,000 PER JOB.

SOLUTION: REDUCE THE JOB CREATION BENEFIT PERIOD FOR THE FEDERAL EZ PROGRAM TO 7-10 YEARS, BRINGING IT IN LINE WITH OTHER TYPES OF FEDERAL INITIATIVES. ALSO, CAP THE YEARLY TAX CREDIT AMOUNT PER JOB TO SOMETHING LIKE $2,000 - $3,000. OUR EXPERIENCE IN MINNESOTA DEMONSTRATES THAT THESE AMOUNTS AND BENEFIT PERIODS WOULD BE MORE THAN ADEQUATE INCENTIVE OR REWARD FOR JOB CREATION. ANY ADDITIONAL BENEFIT COULD BE TIED TO JOB TRAINING.

E. PROBLEM: THE CURRENT FEDERAL PROPOSALS DO NOT SET A CAP ON TOTAL PROGRAM COSTS IN TAX EXPENDITURES. EVEN THE BUDGET FIGURES ARE ESTIMATES OF WHAT BUSINESSES MIGHT DRAW DOWN IN A FEDERAL PROGRAM.

DISCUSSION: OUR EXPERIENCE IN MINNESOTA HAS SHOWN US THAT IT IS POSSIBLE TO CAP AN ENTERPRISE ZONE PROGRAM WITHOUT CRIPPLING IT AND WITHOUT CREATING A HUGE BUREAUCRACY TO ADMINISTER IT EFFECTIVELY. SO LONG AS QUESTIONS REMAIN ABOUT WHETHER OR NOT EZ PROGRAMS PAY FOR THEMSELVES THROUGH A TRUE INCREASE IN INCOME TAX REVENUE AND OTHER RELATED REVENUE/EXPENSE IMPACTS, AND SO LONG AS QUESTIONS REMAIN ABOUT WHETHER PROPOSED FEZ BENEFITS ARE MORE THAN NECESSARY TO STIMULATE JOB CREATION AND INVESTMENT, WE BELIEVE IT IS PRUDENT TO SET LIMITS ON THE PROGRAM AND SET UP AN EXCITING INTERGOVERNMENTAL PARTNERSHIP THAT EMPHASIZES LOCAL CONTROL.

SOLUTION: IN ADDITION TO THE ABOVE RECOMMENDATION TO DECREASE THE EMPLOYER JOB CREATION TAX CREDIT BENEFIT PERIOD AND PUT A YEARLY CAP ON IT PER JOB, WE RECOMMEND A CAP ON THE OVERALL FEDERAL PROGRAM AND ON EACH ZONE. THE LOCAL MUNICIPALITIES COULD THEN, SUBJECT TO FEDERAL LIMITS, DECIDE HOW BEST TO UTILIZE THE PROGRAM IN THEIR OWN ZONES, MAKING SUCH DECISIONS AS THE FOLLOWING:

- INVESTMENT THRESHOLDS FOR BUSINESS PARTICIPATION
- TAX CREDIT DOLLARS PER JOB CREATED RATIOS OR REQUIREMENTS.
- WHETHER TO EMPHASIZE BUSINESS RETENTION, EXPANSION OR CREATION.
- WHETHER TO TIE-IN OTHER GERMANE COMPONENTS SUCH AS WORKER TRAINING, CHILD CARE AND HOUSING.

THIS TYPE OF PARTNERSHIP AND FLEXIBILITY CAN MAXIMIZE THE EFFECTIVENESS OF THE PROGRAM AND MINIMIZE THE COSTS WHILE INCREASING LOCAL CONTROL WITHOUT CREATING A BLOATED BUREAUCRACY.

THEN, AFTER THE FEDERAL GOVERNMENT GAINS EXPERIENCE WITH THE PROGRAM, IT CAN DECIDE WHETHER BENEFITS ARE ADEQUATE TO ACCOMPLISH THE PROGRAM'S GOALS, AND IT CAN STUDY AND DECIDE IF THE PROGRAM TRULY PAYS FOR ITSELF AND, IF SO, WHETHER THE CAP SHOULD BE RAISED OR ELIMINATED.

WE THINK IT WOULD BE EASIER TO RAISE BENEFITS, IF IT APPEARS JUSTIFIED, THAN TO LOWER THEM, IF THEY PROVE TO BE EXCESSIVE. WE THINK THAT WITH THE SOMEWHAT LOWER BENEFITS RECOMMENDED HERE AND A CAP, THE PROGRAM CAN BE VERY SUCCESSFUL ESPECIALLY IF IT IS COMBINED WITH AN INTERGOVERNMENTAL PARTNERSHIP THAT MAXIMIZES LOCAL PARTICIPATION AND CONTROL. WE IN MINNESOTA OFFER OUR SUPPORT IN WHATEVER WAY WE MAY TO ASSIST CONGRESS OR HUD IN INCORPORATING OUR RECOMMENDED CHANGES INTO THE PROPOSED FEDERAL PROGRAM.

IN MINNESOTA, WE BELIEVE THE PROGRAM DOES PAY FOR ITSELF AND DOES RESULT IN GENUINELY NEW ECONOMIC ACTIVITY; BUT WE REALIZE THAT THE HARD DATA IS ONLY BEGINNING TO COME IN.

F. WE WOULD LIKE TO ADD TWO FINAL COMMENTS OR RECOMMENDATIONS:

- CURRENT PROPOSED LEGISLATION PERMITS A QUALIFYING EMPLOYEE TO CLAIM INCOME TAX CREDITS OF 5% OF NEW WAGES IN A ZONE WITH THE DRAWDOWN IN ANY ONE YEAR LIMITED TO THE INDIVIDUALS TAX LIABILITY. SINCE MANY OF THESE PEOPLE HAVE LOW AND MODERATE WAGES, THEIR INCOME TAX LIABILITIES WILL BE SLIGHT. WE RECOMMEND THAT INSTEAD OF A CARRY FORWARD PROVISION FOR THESE PEOPLE, THEY BE ALLOWED A REFUND FROM THEIR ELIGIBLE CREDITS EVEN IF IT EXCEEDS THEIR TAX

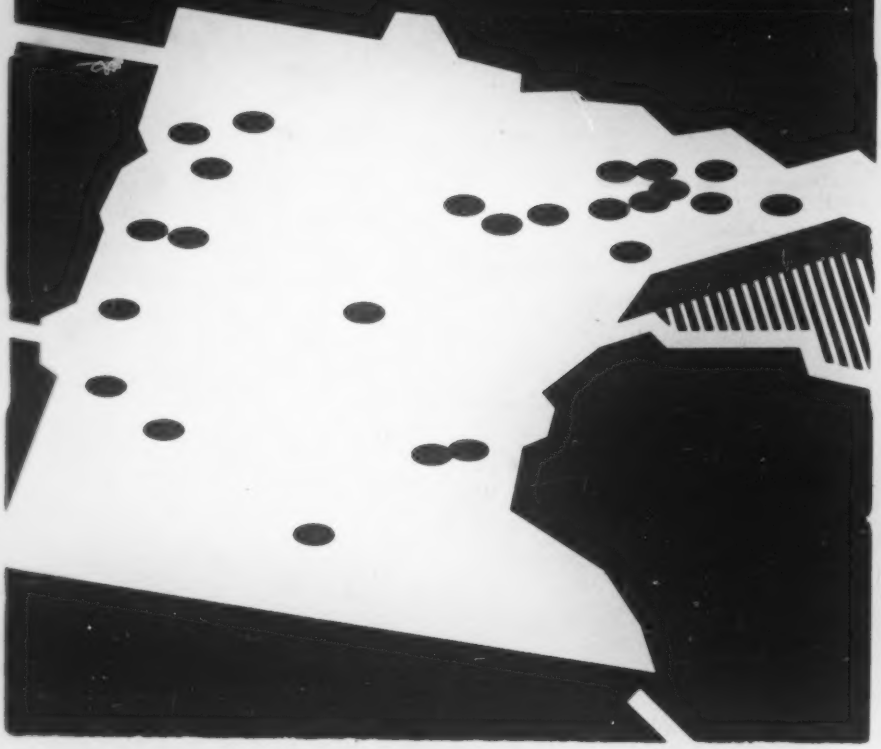
LIABILITY IN ANY PARTICULAR YEAR. THEIR MEANS ARE LIMITED AND THE EFFECT ON THE TREASURY WOULD BE NEGLIGIBLE.

- WE ENCOURAGE THE COMMITTEE TO GIVE SERIOUS CONSIDERATION TO RURAL ENTERPRISE ZONE PROPOSALS. THIRTY-THREE RURAL DESIGNATIONS ARE FAR TOO FEW IN THIS COUNTRY, PARTICULARLY IF INDIAN NOMINATIONS ARE INCLUDED IN THE RURAL COMPETITION. WE BELIEVE THAT THE DESIGNATIONS SHOULD BE SUBSTANTIALLY INCREASED AND/OR THAT CLUSTERS OF RURAL AREAS BE ALLOWED TO APPLY AS ONE PROPOSED ZONE.

SPEECHES/5-(1,4)

MINNESOTA ENTERPRISE ZONE

STATUS REPORT 1987



MINNESOTA ENTERPRISE ZONE
STATUS REPORT 1987

July, 1988

Minnesota Department of
Trade and Economic Development

900 American Center Building
150 East Kellogg Boulevard
St. Paul, Minnesota 55101

612/ 296-5005

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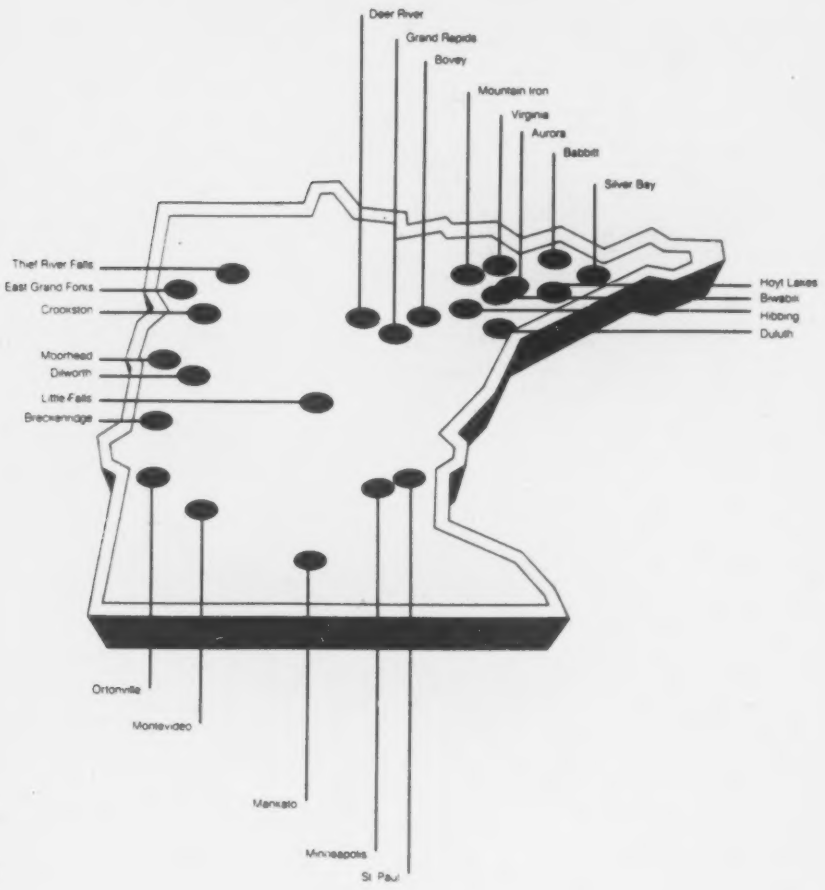
Minnesota Enterprise Zone Locations



Summary

In 1987, Enterprise Zone cities reported that 1,440 new jobs were created as a result of the Minnesota Enterprise Zone Program. Of the new workers, 863 were disadvantaged. This is a significant enhancement of the state's ongoing efforts to stimulate new investment in Minnesota's distressed areas.

1987 was the fourth full year of the Enterprise Zone Program. Considerable effort by participating municipalities, the Minnesota Department of Trade and Economic Development (DTED) and the Minnesota Department of Revenue was expended to implement this flexible and powerful economic development tool. The Enterprise Zone Program continued to serve as a catalyst for increased communication and cooperation between Revenue and DTED in the use of taxation policy for economic development purposes. However, the 1987 Legislature reduced the role of the Department of Revenue in the Enterprise Zone Program by transferring program responsibility to DTED.

1987 Enterprise Zone Program highlights include:

- 877 businesses awarded tax credits - 824 in border city zones and 53 in competitive cities, an increase of 159 over 1986.
- $7,400,549 in state-paid tax credits awarded.
- $4,052,670 in local contributions made by participating municipalities.
- 7,901 jobs retained.
- 1,440 jobs created (full-time equivalents) of which 863 were filled by economically disadvantaged people.

Introduction

The purpose of the Minnesota Enterprise Zone Program is to address the fiscal disparity in Minnesota's border cities and economic distress in the state's urban, agricultural and iron mining areas. State tax policy is used to stimulate job creation and private investment in these locations. [MS 469.166]

Enterprise Zones are geographically defined areas in which state and local tax credits and refunds are available to encourage business retention and development. They are unique among economic development programs in that the basic eligibility criterion is the location of the business rather than its size, financial status and, in most respects, the nature of its operations.

The Enterprise Zone Program provides state tax credits to a business; and may be considered a reward for a business when it achieves its development objectives within a distressed area. This reward concept distinguishes the Enterprise Zone program from other types of public business financing. These tax credits are frequently referred to as a grant to a business because, in most cases, there is no repayment required.

In 1983, the Minnesota Legislature set aside $32 million in forgone tax revenues over an eight year period for a state-funded Enterprise Zone Program for border and competitive cities. In 1984, the Legislature set aside $3.6 million more for the program. The 1985 Legislature added $800,000 specifically for the five cities on the eastern Mesabi Iron Range, an area that now includes the greatest concentration of Enterprise Zones. The 1986 Legislature added $600,000 - $200,000 for Biwabik and $400,000 for a competitive statewide pool. In 1987, $2 million was added for division on a per capita basis between those border cities on the state's western border, bringing the total amount of taxes to be forgone over the life of the program to $39 million.

Program Highlights

Border City Program

The Border City Program is intended to promote economic development by reducing the difference between the costs of doing business in Minnesota and in neighboring states, a problem known as a fiscal disparity. The main goal of this program is equalization—tax reductions to keep existing businesses in Minnesota—with secondary emphasis on the creation of new development. Businesses located throughout the city are eligible to receive state property and income tax credits if they remain in the border city.

The entire city is a part of the Enterprise Zone, and property tax and job credits may be distributed to existing businesses located throughout the city. New or expanding businesses locating or already located in special target areas within border cities may be eligible for additional credits. These credits are comparable to what is available to a new or expanding business in a competitive city Enterprise Zone.

Competitive Cities

The main goal of the Competitive Zone Program is to encourage new economic growth and new job creation in distressed areas. These areas of distress are often confronted by development constraints, and a good deal of lead time is required for competitive cities to successfully market potential sites to eligible business users.

Like the Border City Program, competitive cities may distribute tax credits only to new or expanding businesses within a designated 400-acre Enterprise Zone, usually an industrial, commercial or service-oriented area of the city. These Enterprise Zone sites are the only locations eligible for the distribution of state and local Enterprise Zone tax credits.

Restrictions

To be eligible to receive Enterprise Zone tax benefits, a business may not be of the following business type:

1. A facility for which the primary purpose is one of the following: the provision of recreation or entertainment; a private or commercial golf course, country club, massage parlor, tennis club, skating facility including roller skating, skateboard and ice skating; racquet sports facility including a handball or racquetball court, hot tub facility, suntan facility or racetrack.
2. Owned by a public utility.
3. Used in the operation of a financial institution.
4. Owned by a fraternal or veterans' organization.
5. Owned by a retail food or beverage service business operating under a franchise agreement requiring the business to be located in the state.

Enterprise Zone Incentives

Crucial to an Enterprise Zone's success in retaining or creating economic development is the quality of the incentives available through the program.

There are four state-paid tax credits allowed for business expansion or new business investment in border city and competitive city Enterprise Zones:

1. A state-paid property tax credit for a portion of a new eligible business or the additional property taxes incurred by the expansion of an existing business in the zone.
2. An income tax credit for a portion of the cost of debt financing used to construct new facilities.
3. An income tax credit of up to $3,000 annually to an employer for each additional worker employed in the zone (excluding construction workers).
4. Exemption from the general sales tax for purchasing construction materials or equipment for use in the zone. The tax is fully paid and reimbursed as an income tax credit.

Businesses throughout a border city are eligible for two additional types of state tax credits:

1. A credit against an employer's income tax up to $1,500 per year for each existing employee (usually awarded based on a percentage of the business's workers' compensation costs).
2. A state-paid property tax credit for a portion of the property tax on an existing commercial or industrial facility.

The 1984 Legislature amended the Enterprise Zone law to allow the refund of state income tax credits, making the program more attractive to start-up companies, which typically do not have income tax liabilities.

Anti-Pirating Provision

The Minnesota Legislature has stipulated that Enterprise Zone benefits are not available to a business if the construction or improvement of the business facility is likely to have the effect of transferring existing employment from other municipalities within the state. This "anti-pirating" provision is strictly applied by the Minnesota Department of Trade and Economic Development in the evaluation of Enterprise Zone credit applications.

Local Contribution Tax Credits

Enterprise Zone cities must provide a qualifying local contribution to each business receiving state credits. These contributions usually consist of local property tax reductions for five years in the form of a property tax reduction for employment property, or an alternative contribution or investment from other municipal funds (excluding any special federal grants or loans), such as public facility improvements, equivalent to the property tax reduction. This local contribution is most often the reclassification of the commercial or industrial property as Class 3b "Employment Property" [MS 273.13 Subd. 24(b)].

Employment property shall be valued and assessed at 45 percent of the first $50,000 of market value and 50 percent of the remainder. For employment property located in border cities, the first $80,000 of market value shall be valued and assessed at 60 percent and the remainder shall be assessed and valued at 86 percent.

At the option of the business and the city, the business may receive local and state tax credits or local property tax reduction only. State tax credits must be applied for annually and are available to an eligible business for up to five years in a competitive city or up to seven years in a border city.

Each locality has the flexibility to negotiate with the business for the types and amounts of credits to be provided, thus tailoring the program to meet the business's particular needs.

Tax Credit Allocations

The Minnesota Legislature has set aside $39 million in taxes to be forgone over the eight year life of the Enterprise Zone Program. The following is the distribution of this allocation to the 16 Minnesota Enterprise Zones:

Border city seven year allocations:

City	Total (Seven Years) Allocations
Breckenridge	$ 988,455.37
Dilworth	654,847.55
Duluth	6,810,940.00
East Grand Forks	2,144,033.48
Moorhead	7,563,925.05
Ortonville	648,738.55
Subtotal	**$18,810,940.00**

Seven year allocations for competitive cities:

City	Total (Seven Years) Allocations
Aurora, Babbitt, Biwabik	$ 1,000,000
Hoyt Lakes and Silver Bay	
Crookston	900,000
Grand Rapids, Bovey, Deer River and Bass Brook Township	800,000
Hibbing	800,000
Little Fall	900,000
Mankato	2,500,000
Minneapolis	4,500,000
Montevideo	800,000
St. Paul	4,500,000
Thief River Falls	1,750,000
Virginia/Mountain Iron	$ 1,750,000
Subtotal	**$ 20,200,000**
Total	**$ 39,010,940**

1987 Status Report

Businesses Served

In 1987, 877 businesses in border cities and competitive city zones applied for and received Enterprise Zone credits.

Border Cities	Number of City Businesses Served
Breckenridge	73
Dilworth	39
Duluth	2
East Grand Forks	97
Moorhead	488
Ortonville	125
Total	**824**

Border cities allocated business retention credits almost exclusively to existing businesses for the purpose of retaining employment.

Competitive Zones

City	Number of Businesses Served
Aurora	2
Babbitt	2
Crookston	1
Grand Rapids/West Range	3
Hoyt Lakes	1
Hibbing	0
Little Falls	3
Mankato	7
Minneapolis	6
Montevideo	5
St. Paul	8
Thief River Falls	6
Virginia/Mountain Iron	9
Total	**53**

State-Paid Tax Credits Granted

During 1987, a total of $7,400,411 in state-paid credits was allocated by border and competitive city Enterprise Zones. Border cities awarded $2.5 million, or 34 percent, and competitive cities awarded $4.8 million, or 66 percent.

Zone Type	1984 - 1986 Credits Awarded	1987 Credits Awarded
Border Cities	$11,518,747	$ 2,502,138
Competitive Cities	5,053,097	4,898, 411
Totals	**$16,571,844**	**$7,400,549**

Border City Program

Border Cities awarded $2,502,138 in state tax credits primarily as employment and property tax credits for the retention of businesses within the state.

City	1984 - 1986 Credits Awarded	1987 Credits Awarded
Breckenridge	$287,816	$106,746
Dilworth	284,409	94,450
Duluth	6,610,940	200,000
East Grand Forks	1,050,569	357,107
Moorhead	3,179,045	1,348,669
Ortonville	105,968	395,669
Totals	**$11,518,747**	**$2,502,138**

Competitive City Program

Competitive cities awarded $4,996,705 in state tax credits in 1987 primarily as new employment and debt financing income tax credits. These credits reward new job creation and assumption of debt for building construction, improvement, expansion and acquisition, and for machinery and equipment acquisition.

Distribution of state tax credits by competitive city Enterprise Zones:

City	1984 - 1986 Credits Awarded	1987 Credits Awarded
Aurora	$61,630	$30,000
Babbitt	10,616	188,000
Crookston	800,000	100,000
G. Rapids/W. Range	55,352	123,011
Hibbing	375,000	0
Hoyt Lakes	0	74,710
Little Falls	255,013	368,487
Mankato	428,987	1,023,940
Minneapolis	768,787	1,937,602
Montevideo	64,000	199,900
St. Paul	984,588	649,483
Thief River Falls	881,106	28,219
Virginia/Mountain Iron	368,018	175,059
Totals	**$5,053,097**	**$4,898,411**

Credit Use by Type, 1987
All Enterprise Zone Cities

- Debt Financing (39.2%)
- Employment (29.2%)
- Property Tax (19%)
- Sales Tax (12.6%)

Credit Use by Type, 1987
Border Cities

- Debt Financing (11.8%
- Employment (38%)
- Property Tax (49.5%)
- Sales Tax (.7%)

Minneapolis provided $1,937,602 of all state tax credits awarded by competitive city Enterprise Zones, followed by Mankato with $1,221,220.

All Enterprise Zone City Use by Type of Credit

The accompanying credit summary table displays the extent to which each of the state credits was used by Enterprise Zone cities in 1987. The accompanying pie charts display the percentage use of each credit. As can be seen by these displays:

- The debt financing credit made up the highest amount — 39.2 percent ($2,901,893).
- The employment credit comprised 29.2 percent ($2,157,403) of all state credits granted in 1987.
- The state-paid property tax credit comprised 19 percent ($1,406,382).
- The sales tax credit made up 12.6 percent ($934,871).

The debt financing credit, the most heavily used state paid tax credit, comprised $2,901,893 or 39 percent of all state paid tax credits provided in 1987. The percentage increase in the debt financing and the percentage decrease in the state-paid property tax credit since 1985 reflect the growing impact of both the border and competitive cities' use of the state tax credits for new job creation and business expansion and development.

Border City Use by Type of Credit

The accompanying credit summary table and pie chart display the extent to which each of the state credits was used by border city Enterprise Zones in 1987. As can be seen:

- The state-paid property tax credit comprised 49.5 percent ($1,236,640).
- The employment credit comprised 38 percent ($951,261) of all state credits provide by Border Cities in 1987.
- The debt financing credit comprised 11.8 percent ($295,877).
- The sales tax credit made up .7 percent ($18,360).

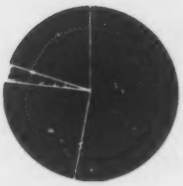
The heavy use of the state-paid property tax credit and the employment credit can be attributed to the business retention policies of the border Enterprise Zones. During 1987, Enterprise Zone tax credits were predominantly used to retain existing businesses.

Competitive City Use by Type of Credit

The accompanying credit summary table and pie chart display the extent to which each of the state credits was used by competitive city Enterprise Zones in 1987. As can be seen:

- The debt financing credit comprised 53.2 percent ($2,606,016).
- The employment credit comprised 24.6 percent ($1,206,142) of all state credits granted in 1987.
- The sales tax credit made up 18.7 percent ($916,511).
- The state-paid property tax credit comprised 3.5 percent ($169,742).

Competitive cities awarded credits for new job creation and as rewards for business investments, particularly when a business assumed new debt to finance an investment in fixed assets. The small use of the state-paid property tax credits indicates the lesser importance of this credit in relation to the ease with which the income tax credits can be immediately drawn based on the achievement of agreed-upon investment and job creation performance objectives.



Credit Use by Type, 1987
Competitive Cities

- Debt Financing (53.2%)
- Employment (24.6%)
- Property Tax (3.5%)
- Sales Tax (18.7%)

Local Contributions

During 1987, participating municipalities pledged or made investments totaling $4,052,670. The 1987 local contribution for border city zones was $458,206, and the contribution for competitive city zones was $3,594,464. Although the majority of local contributions came from property tax reductions, increasing amounts have come from alternative sources, primarily in the form of public works improvements and land, lease or assessment reductions.

Jobs Retained

The accompanying employment table depicts job retention and job creation information for border and competitive zones. Border cities may use Enterprise Zone credits to retain businesses and the accompanying employment. During 1987, border cities reported retaining 5,922 jobs, of which 2,991 were in Moorhead, 1,498 were in East Grand Forks and 511 were in Ortonville. The border cities generally reported a job as retained if the employing business received Enterprise Zone credits and remained within the city. No analysis has been completed which identifies only those jobs which would have been lost to the state if Enterprise Zone credits had not been granted to a particular business within a Minnesota border city. In addition, competitive cities reported retaining 1,979 jobs with Minneapolis claiming 791 of this total.

Jobs Created

During 1987, participating municipalities reported that 1,440 new jobs were created by private businesses using Enterprise Zone credits. Little Falls reported 369, or 25 percent, of the new jobs created; Saint Paul had 291; Mankato had 156; Thief River Falls had 110; and Babbitt had 78. By and large, the new jobs were created in manufacturing operations.

Disadvantaged Workers Hired

During 1987, 863 people classified locally as "disadvantaged" were hired to fill positions created in the zone. The majority of these people, 340, were hired in Little Falls. Disadvantaged workers have been defined as workers who had been unemployed until hired by the business receiving Enterprise Zone credits.

Average Wage per New Job Created

The average wage for the 1,440 new jobs created was $13,358 per year. The highest average wage paid was $22,264 in Minneapolis and the lowest, $9,152,was in Ortonville. By and large, this wage range provides low- and moderate-income jobs.

Job Retention and Job Creation by Municipality

Municipality	Number of Applications	Number of Retained Employees	Number of New Employees	Average Wage Per Job Created	Number of Disadvantaged Workers Hired
Border Enterprise Zone					
Breckenridge	73	369	2	$10,400	2
Dilworth*	39	310	14	13,250	12
Duluth*	2	243	75	17,500	30
East Grand Forks	97	1,498	0	N/A	0
Moorhead*	488	2,991	88	10,283	N/A
Ortonville*	125	511	N/A	9,152	20
Subtotal	**824**	**5,922**	**179**	**$12,117**	**64**
Competitive Enterprise Zone					
Aurora*	2	0	10	$13,520	6
Babbitt	2	0	78	17,160	71
Biwabik	0	0	0	N/A	0
Crookston*	1	55	60	14,560	50
G.Rapids / W. Range	3	N/A	31.4	9,700	4
Hibbing	0	0	0	N/A	0
Hoyt Lakes*	1	0	10	14,560	6
Little Falls*	3	0	369	11,648	340
Mankato*	7	190	156	16,050	145
Minneapolis	6	791	30	22,264	14
Montevideo*	5	0	44	14,560	N/A
St. Paul	8	255	291	16,102	43
Silver Bay	0	0	0	N/A	0
Thief River Falls	6	484	110	11,700	107
Virginia / Mt. Iron*	9	204	71.5	13,356	13.5
Subtotal	**53**	**1,979**	**1,261**	**$14,598**	**880**
Total	**877**	**7,901**	**1,440**	**$13,358**	**863.5**

** Municipalities which have committed all state credits*
N/A = Not Available

State and Local Tax Credit Distribution

Municipality	Number of Applications	State Paid Property Tax Credits	State Paid Job Credit	State Paid Sales Tax Credit	State Paid Debt Financing Credit	Tax Credits Authorized In 1987	Local Contribution
Border Enterprise Zone							
Breckenridge	73	$ 43,534	$ 56,323	$ 2,289	$ 4,600	$ 106,746	$ 16,823
Dilworth*	39	32,400	59,425	0	2,625	594,450	10,000
Duluth*	2	0	0	0	200,000	200,000	120,000
East Grand Forks	97	136,988	218,967	0	1,152	357,107	N / A
Moorhead*	488	806,997	448,386	5,786	87,500	1,348,669	300,288
Ortonville*	125	216,721	168,160	10,285	0	395,166	11,095
Subtotal	**824**	**$1,236,640**	**$ 951,261**	**$ 18,360**	**$ 295,877**	**$2,502,138**	**$ 458,206**
Competitive Enterprise Zone							
Aurora*	2	$ 0	$ 30,000	$ 0	$ 0	$ 30,000	$ 10,815
Babbitt	2	6,000	54,000	0	128,000	188,000	168,840
Biwabik	0	0	0	0	0	0	0
Crookston*	1	0	100,000	0	0	100,000	40,294
G.Rapids / W. Range	3	0	24,098	31,635	67,278	123,011	47,470
Hibbing	0	0	0	0	0	0	0
Hoyt Lakes*	1	0	36,000	10,070	28,640	74,710	33,548
Little Falls*	3	0	352,000	7,730	8,757	368,487	49,938
Mankato*	7	0	142,720	65,375	815,845	1,023,940	121,109
Minneapolis	6	132,974	202,500	749,647	852,481	1,937,602	2,489,716
Montevideo*	5	0	132,000	10,900	57,000	199,900	N / A
St. Paul	8	9,533	45,000	0	594,950	649,483	588,152
Silver Bay	0	0	0	0	0	0	0
Thief River Falls	6	0	22,620	5,599	0	28,219	4,047
Virginia / Mt. Iron*	9	21,235	65,204	35,555	53,065	175,059	40,535
Subtotal	**53**	**$ 169,742**	**$1,206,142**	**$916,511**	**$2,606,816**	**$4,898,411**	**$3,594,464**
Total	**877**	**$1,406,382**	**$2,157,403**	**$934,871**	**$2,901,893**	**$7,400,549**	**$4,052,670**

** Municipalities which have committed all state credits*
N / A = Not Available

Marketing/Training

Brochures on the Enterprise Zone program were developed by the Department of Trade and Economic Development, which also included the program in its overall marketing material.

During 1987, the State of Minnesota continued as a board member of the American Association of Enterprise Zones, a national organization of public and private sectors interested in both state and national Enterprise Zone programs and policies. State staff participated in an Enterprise Zone seminar held in South Bend, Indiana, and sponsored by the North Central Council of the National Association of Housing and Redevelopment Officials (NAHRO).

1987 Legislative Actions

No actions regarding the Enterprise Zone program were taken by the Minnesota Legislature in 1987.

Contact the Enterprise Zone cities directly for local guidelines, applications and enterprise zone maps.

Border Cities

Wayne Oberg
City of East Grand Forks
304 4th Street NW
East Grand Forks, MN 56721
218/773-2483

Marshall Weems
City of Duluth
Room 400, City Hall
Duluth, MN 55802
218/723-3556

Forest "Skip" Carpenter
City of Breckenridge
420 Nebraska
Breckenridge, MN 56520
218/643-1173

Economic Development Director
City of Ortonville
33 NW 2nd Street
Ortonville, MN 56278
612/839-2618

Stan Thurlow
City of Dilworth
107 Center Avenue East
Dilworth, MN 56529
218/287-2313

Beth Grosen
City of Moorhead
500 Center Avenue
Moorhead, MN 56560
218/299-5441

Competitive Cities

Larry Forsythe
City of Mankato
202 East Jackson
Mankato, MN 56001
507/625-3161, ext. 256

Jane Hause
Minneapolis Comm. Dev. Agency
331 Second Avenue South
Minneapolis, MN 55415
612/342-1377

Don Stewart
City of Thief River Falls
Box 528
Thief River Falls, MN 56701
218/681-2500

Steve Mercil
Crookston Jobs Inc.
P.O. Box 492
Crookston, MN 56716
218/281-7979

Patricia Spence
Community Development
of Little Falls
P.O. Box 356
Little Falls, MN 56345
612/632-5466

John Campobasso
St. Paul Port Authority
1900 Amhoist Tower
345 St. Peter Street
St. Paul, MN 55102
612/224-5686

City Planner
City of Virginia
City Hall
Virginia, MN 55692
218/749-2938

Bill Beck
City of Mt. Iron
City Hall
Mt. Iron, MN 55768
218/735-8267

A.J. Johnson
City of Montevideo
P.O. Box 676
Montevideo, MN 56265
612/269-6575

Frank Bigelow
City of Hibbing
City Hall
East 21st and 4th Avenue E.
Hibbing, MN 55746
218/262-3486

Curt Antilla
City of Aurora
City Hall
Aurora, MN 55705
218/229-3671

Duane Northagen
City of Silver Bay
Silver Bay, MN 55614
218/226-4444

Gerald O'Donnell
City of Hoyt Lakes
City Hall
Hoyt Lakes, MN 55750
218/225-2344

Newell Cedarholm
City of Babbitt
City Hall
Babbitt, MN 55706
218/827-3464

Joe Wood
Grand Rapids, Bovey, Deer River
and Bass Brook Township
501 Second Ave NW
Grand Rapids, MN 55744
218/327-2241

Mark C. Flaherty
City of Biwabik
P.O. Box 529
Biwabik, MN 55708
218/865-4183

Minnesota Department of
Trade and Economic Development

Community Development Division

900 American Center
150 East Kellogg Boulevard
St. Paul, MN 55101-1421

612/296-5005
Fax: 612/296-1290

August 9, 1989

The Honorable Charles E. Grassley
United States Senator
c/o Tracy Crowley
Hearing Clerk
Senate Committee on Small Business
Room 428A, Russell Senate Office Building
Washington, D.C. 20510-6350

Dear Senator Grassley:

Senators Rudy Boschwitz and Joseph Lieberman have been kind enough to forward several questions from you which further explore our written and oral testimony from Minnesota on enterprise zones given to the Small Business Committee on June 21, 1989. After taking your questions under consideration, I offer the following responses:

Question 1:

"The point can be made that businesses from right outside the federal enterprise zone boundary could relocate inside the zone. This could have the effect of weakening the outside area without benefiting the entire region.

Do you agree with this point, and if so would you support adding a provision to the federal program preventing a business from abandoning a facility solely to relocate within a federal enterprise zone?"

Response:

Yes, as we stated in our testimony, we agree this could happen and we support adding a provision to the federal program preventing a business from abandoning a facility solely to relocate within a federal enterprise zone.

The Minnesota enterprise zone program prohibits both the pirating of businesses between municipalities and the awarding of enterprise zone benefits to any business abandoning a property within a municipality unless it can sell or rent the facility it's vacating to another business. We think there should be exceptions such as when a business is land locked and must move out of its facilities in order to grow, expand or modernize. Exceptions should also be allowed for compelling and well documented business necessities such as unsolvable infrastructure problems or business consolidations.

Since we think exceptions should be allowed, we believe it is important that this facet of the enterprise zone program be monitored; the appropriate body to perform this oversight function is the state government where the enterprise zone is located.

Question 2:

"The point will also be made that businesses could leave the federal enterprise zone without penalty after a few years of drawing down the enterprise zone benefits.

Would you support instituting penalties if a business withdraws from an enterprise zone soon after the benefits have expired?"

Response:

We believe that there should be penalties for businesses that leave an enterprise zone soon after drawing down benefits. This is especially true for the proposed federal program (HR6/S58) where benefits are heavily loaded on the front end. While some proposed benefits such as tax credits for research and new employment wages can be received by businesses on a straight-line basis during their years in an enterprise zone, other substantial benefits can be received immediately or within the first years. These could include the following:

Estimated Time it Takes a Business to Realize all or Most of the Benefit	F.E.Z. Benefit
0-1 year	• a 10% investment tax credit
3 years	• sale of stock to raise capital-aided by the income tax deductibility of enterprise zone stock purchases by the investor
0-1 year	• capital injection aided by special enterprise zone revolving loan funds
3-7 years	• 50% tax credit on new wages paid for employment of disadvantaged workers, scaling down to 10% by year seven
3-7 years	• accelerated cost recovery deduction for tax-exempt bonds going for qualifying enterprise zone construction property

This list shows substantial front-end benefits that become depleted for a business over a three to seven year period, reducing the incentive to stay in a zone.

In Minnesota we have dealt with this problem by making some or all enterprise zone benefits subject to repayment if a business leaves a zone within two years of drawing benefits. If it leaves within six months after drawing credits, it is subject to repaying 100% of benefits received. The percentage subject to repayment goes down by 25% every six months so that after two years a business could move out without penalty. Since our enterprise zone program gives benefits for only five years, a maximum of five years' benefits would have to be repaid.

Federal penalties for leaving a federal enterprise zone would probably need to be structured differently, in part because of the longer benefit period, and because the federal program contains more substantial benefits. In particular, care must be taken so that penalties aren't so great that it prevents businesses from becoming involved in the program.

One way to structure federal penalties is suggested here: businesses ceasing to operate in a zone or transferring operations substantially out of a zone within three years of receiving zone benefits (or enterprise zone tax reductions) would have to repay benefits according to the following schedule:

Termination or Transfer of Operations	Repayment Requirement
Within 1 year of receiving benefits	Last 2 years of benefits received
Between 1-2 years of receiving benefits	Last 1 year of benefits received
After 2 years	No repayment required

Care would need to be given in determining which benefits count in figuring the last year of benefits received. Would it be just tax reductions or would it include years in which revolving loan funds were still being repaid? Would it include years a preferred procurement contract was still in effect?

In Minnesota, local governments are required to inform the state if a possible repayment situation exists due to a business terminating or transferring operations. We do not rely on businesses to "turn themselves in." We believe that local government is the only level of government capable of monitoring business operation status effectively. We believe further that this oversight function is important in protecting the enterprise zone program - not from the majority of businesses that are conscientious and responsible, but from the minority that could try to take unfair advantage of the program.

Question 3:

"A recent study done by Professor Dennis Grady, formerly of the University of Northern Iowa, entitled "The Second War Over the States," concluded that tax credits have absolutely no influence on business location. Professor Grady also concluded that the labor force is one of the most important factors, including the education of the population.

Could you comment on these findings?"

Response:

In preparing a response to Professor Grady's study, my staff was in touch with him to be sure we had gotten the right study to review. The study is entitled, "State Economic Development Incentives: Why do States Compete?" and was published in the fall 1987 issue of "State and Local Government Review."

Contrary to Mr. Grady's assertion that state tax incentives don't work, we know that state tax credits are definitely one factor in business decision making because we're frequently contacted by businesses requesting this information. Business decision making is largely a "least-cost" process. Businesses tend to locate where it costs the least to do business. Obviously then, businesses consider tax incentives because they reduce the cost of doing business.

Professor Grady assumes in his study that incentives don't create new economic activity or jobs, but he provides no data to support his assumption. We know this is wrong because in our economic development programs we examine the financial status of each business to determine that public aid is necessary before providing grants or loans. We know from this that our financial aids are creating genuinely new jobs and economic activity.

Mr. Grady blames the presumed failure of incentives to create new jobs on the states targeting aids to big businesses. We know this is not true of the Minnesota experience. Since 1984, we have helped 221 businesses with loans from our Economic Development Program and Economic Recovery Fund. Sixty percent of the loans have gone to businesses with 50 or fewer employees. The maximum loan is $500,000. These are clearly small business deals.

On the business location issue, our understanding of Grady's study is not that he claims tax credits have no effect on location decisions, but that the effect is a negative one--a "job heist" between states. We have pointed out earlier that we think this should be prohibited by an "anti-pirating" provision in the federal enterprise zone program.

However our experience in Minnesota with incentives leads us to disagree with Mr. Grady again. We have seen two positive effects of incentives on business location decisions. The first is to help businesses remain in distressed areas, thereby anchoring and stabilizing the areas and the second is to influence businesses to locate or expand into distressed areas.

The City of Moorhead is an example of both positive effects. Moorhead (pop. 30,000) shares a metropolitan area with Fargo, North Dakota. Moorhead lost 40-50 businesses to Fargo in a little over a year before it was designated a border city enterprise zone. The businesses left because of reduced operating costs in North Dakota--from lower taxes and lower worker's compensation costs. The enterprise zone program has permitted Moorhead to allocate state tax credits yearly to virtually all of its businesses for staying in the city. The cost of incentives has been small-averaging $400-500 per job retained or about $2,000-3,000 per business per year. A July, 1989 report from Moorhead shows that only eight businesses have moved to Fargo since their enterprise zone program started in 1983 and 65 new businesses have been established. We believe this clearly demonstrates an important aspect of enterprise zones--that they can be used to help businesses stay in their present locations and thereby stabilize economically distressed areas.

In closing, Senator Grassley, I want to thank you and the committee for the opportunity to provide input on a program that the state strongly supports. I hope this letter helps provide a "pro-enterprise zone" perspective on the points raised by Professor Grady. If I can be of further service, be sure to let me know.

Sincerely,

Louis F. Jambois, Director
Community Assistance Unit

LFJ:km
SCDP.EZ/I14-(1-5)

cc: Senator Rudy Boschwitz
Senator Joseph Lieberman

Senator LIEBERMAN. Thank you both very much for your testimony. It was very helpful, and right on point.

I welcome Senator Tom Harkin from Iowa. Do you have a statement you would like to make?

STATEMENT OF HON. TOM HARKIN, A U.S. SENATOR FROM THE STATE OF IOWA

Senator HARKIN. No. I just reserve anything for the record, Mr. Chairman. Thank you very much for your kindness. I appreciate being here.

Senator LIEBERMAN. Thank you. I will begin the questioning, then Senator Boschwitz and I can go back and forth.

Let me begin by setting the political context, if I can. This is an idea that has been around for a while. It is not an old idea, it is still fresh, but my sense of it is, having just arrived here as a Member of the Senate, that it is gaining momentum.

Certainly if you look at the people involved, the original congressional co-sponsor Jack Kemp now is Secretary of HUD and in a position to implement and be a strong advocate for the program. Congressman Rangell now emerges as a major House sponsor and he is a high-ranking Member of the House on the Ways and Means Committee, which has traditionally been opposed, and the Senate, I am reminded by my colleague Senator Boschwitz, has previously passed Enterprise Zone legislation.

So there is something bubbling here and I suppose the closer this all gets to reality the more demanding the questions that are going to be asked of people like us who advocate this program and people like you who are in the field.

The major question, undoubtedly will be, is it worth it? In other words, particularly in the context of the Federal deficit and limited public resources, is there an adequate pay-off for the tax loss that the Government will experience as a result of some of the tax credits and tax incentives.

I would invite all three of you as you desire to respond to that, based if you would on your State experience insofar as you are able to measure it. Because I believe both States have yielded on some State taxes as part of your programs and I wonder whether you feel it has been worth——

Mr. HEINTZ. Well, I will start up. I would say that it is unquestionable that the program has brought significant benefits in the urban areas of Connecticut, where we have the zones.

I would be candid to say as well that these measurements of the job creation and job retention are hard to really say that you can be accurate with. You cannot really understand the business decision and say that absolutely, without any question, the only reason that job was created was because of the Enterprise Zone incentives.

But we can say that those neighborhoods in these cities and I am sure in the rural communities in Minnesota as well, would not have experienced the rate of investment and the rate of job growth that they have experienced with the zone incentive.

So I think that the answer is yes, the program is extremely valuable. The incentives are what make it work. The program has to have the incentives. It has to have some real teeth to really encour-

age investment in areas that otherwise would not get investment, and the program needs to be fairly simple to administer so that you do not overwhelm the businesses with more bureaucracy and paperwork. But if you do those things you can have a measurable impact on the neighborhoods in which you have provided that help.

Mr. JAMBOIS. Thank you, Mr. Chairman. I concur completely. In Minnesota, in our border city zones, we have been able to plot the loss of businesses in distressed areas and the slowdown of the loss of businesses since the zones have been created.

Now, while you may—and we could all conclude at first blush that a border-cities-type zone program does not have applicability to the Federal experience, what it does illustrate is that with incentives you can prevent flight of businesses from distressed areas, those areas of our cities and State that need economic development the most, where the residents need the jobs the most.

While I concur that it is difficult to say that every single one of the jobs created or retained in Minnesota is a direct result of the Enterprise Zone Program, without a doubt I could say that many—a substantial portion of those jobs—would currently not exist in those zones without the program.

We think the cost per job in Minnesota has been very, very low. We think, though we have not plotted this, we believe that the sales and income tax revenue that is generated from those jobs that exist has reduced our costs substantially and that yes, the program is definitely worthwhile.

We look forward to—I should say you authorizing the Enterprise Zone Program when it expires in the next couple of years. We think it is a very important economic development tool.

Senator LIEBERMAN. Mr. Helgesen, did you want to add to that?

Mr. HELGESEN. Yes. I would like to make a couple of comments. The question you have asked is a very tough one to answer with a great deal of certainty and I think that some of the hard data on that is starting to come in.

California recently has come out with a study. New Jersey is on the verge of coming out with a study that is showing quite a bit of economic impact. I would just like to tell you from Minnesota, we have a study that was done two yeas ago by some of our local coordinators.

I did not include it in the testimony because I am not sure that it meets scientific rigors in terms of setting up the study, but I think what they found is very intriguing and that is, they looked at the jobs that had been created through our program and then the income tax revenue that the State would receive from those jobs—and in Minnesota, let me just comment for a second that in Minnesota our benefits can run to a business for a period of 5 years and that is a maximum.

So what they did is, they said well, the jobs have been created. How much tax revenue would Minnesota receive during those 5 years, and they showed that it would be $1.17 for every dollar the State had paid.

Now, when you consider these jobs are permanent and are going to go for, hopefully, many years beyond 5 years, and when you consider that there are many other types of benefits the government will receive—for example, some of these workers had been on

public assistance and now are no longer on public assistance—that is going to be an additional benefit that was not counted.

I think this study really was quite conservative in the conclusions that it came up with and I have talked to Mr. Jambois about trying to repeat a study like this in Minnesota but I think it is very intriguing.

Let me just quickly tell you about one or two examples of communities in Minnesota. Key River Falls, which is up by the Canadian border and is relatively isolated, is a community of 9,000 people that had the Arctic Cap Company go into bankruptcy some years ago and this community of 9,000 people lost somewhere around 1,000 jobs and it was devastating to the community.

They got an Enterprise Zone, where the Enterprise Zone includes mostly commercial industrial and much of which had been occupied by Arctic Cap and they are slowly now, over the last 6 years, worked with a lot of local businesses and tried to attract businesses from surrounding areas and helping business start up expansions and have been able to replace 600 of those 1,000 lost jobs. So it has just been an absolute boon to that town. It has meant a great deal to them.

Senator LIEBERMAN. That is very strong testimony from all three of you and I appreciate it.

Let me follow up with this question, again, one that will be asked of us as this legislation moves along in Congress. You touched on it, all of you, in some measure, but let me ask you to focus in on it.

From your experience in the Enterprise Zones in response to the tax incentives, are we talking about the creation of new jobs or just the relocation of old jobs from one place to another to take advantage of the tax benefits?

Mr. HEINTZ. Sure, it is certainly both, Senator. I mean, it is clear that we are encouraging the investment in targeted areas and those investment decisions might have been made in other areas had there not been special incentives to bring them to the areas in which the zones are located.

So again, I do not think any of us could say with strong scientific evidence that we are actually creating jobs that would not have been created someplace else. But the key is, we are using—this is really a market intervention on the part of Government.

In some cases we use regulatory interventions, in this case we are using tax and financial incentives as an intervention in order to use public policy to accomplish social and public good with private sector investment.

What we see happening is that it is encouraging that investment in areas where the businessman might normally not choose to go for good, sound business reasons—because of the cost of doing business and because of the difficulties of surviving in those neighborhoods—and yet they are doing it because we are providing the incentives.

When they do it, they are providing an improvement to the physical infrastructure of the city or town, they are hiring people from that community, they are contributing to the local tax structure over time, they are contributing to the job base, and what we are seeing now that I think is very exciting, if you link the Enterprise Zone Program with the Family Support Act adopted by this Con-

gress in 1988 and we think about welfare reform, day-care centers, training and education, and employment, as all going on in the zones, we have I think a very exciting combination of social and economic policy.

Mr. JAMBOIS. We attempt, in Minnesota, to absolutely eliminate the movement of jobs from outside a zone into a zone. We try to prevent businesses from moving into a zone just to claim credits.

We believe that jobs are created as a result of the easy program in our State. We believe, also, that in distressed areas jobs are retained. And we think that is of very great value to the State.

Whether or not all of these jobs would have been created anyway is, of course, getting to the point of your question. Some of them, undoubtedly, would be. Some of them, certainly, would not have been created without incentives—tax incentives and local incentives to expand businesses.

Senator LIEBERMAN. If you say it was an acceptable policy, a chief policy goal, an achievement—if we were talking here, and not about new jobs, but just retaining old jobs—in other words, would that be worth the program, if we moved some previously existing jobs into areas where, for other reasons, we thought they were necessary.

Mr. JAMBOIS. That is a two-part question, Mr. Chairman. Part one, I believe the program is valuable in retaining jobs in existing areas of distress. I think that is an important public policy goal that we have had in Minnesota and it has worked very well.

I am not so certain that it would be worth our while to create a program that would move jobs from one location to another.

Senator LIEBERMAN. Mr. Helgesen.

Mr. HELGESEN. Yes, I also have a couple of comments, Senator Lieberman.

As Louie said, and you will find a little discussion of this in our testimony, that in Minnesota we do prohibit businesses, while we prohibit the pirating of businesses from other communities—just flat out, we prohibit it.

We also, if a community, or if a business is going to move into a zone from just outside the zone they have to make a provision to restore the use and value of the facility they have vacated. Otherwise, they cannot receive Enterprise Zone tax credits.

So we really have a pretty tight clamp on business pirating, or switching, or moving to get into the zone.

We found, as I have gotten out and met with some of our coordinators in the field, and I hear the stories about, you know—what happened with this business, or that business? What was their circumstance, or their condition?

I have been impressed with how much that is difficult to quantify and document—yet, is very real.

In the city of Mankato, MI, it got an Enterprise Zone. They had a cabinetmaker that had been in the city for decades. And the two owners were reaching retirement age and no longer wanted to run the business. So they were just letting it wind down.

And their accountant said to them, why do you not try to sell the business and get something out of it. So they tried for 2 years to sell the business and were unable to. I do not know how many prospective purchasers they had, but the numbers did not work.

When the city found out about this and tried to work with the business in the Enterprise Zone, and allowing a potential purchaser to get Enterprise Zone credits, they were able to keep this business from shutting down, and they expanded eventually from 13 businesses originally—or excuse me, 13 employees 3 years ago, up to 38 employees now.

So there is a case where there is clear evidence that we are not just taking jobs from elsewhere. We are creating new economic activity.

Mankato also had a quarry that shut down 5 or 6 years ago because the technology had advanced very rapidly and the company had a lot of old equipment. They were able to work with the two grandsons of the original owners, and with the bank to get them refinanced, and to get that company started again.

And they started with 50—excuse me, they have 50-some employees now in that quarry. And their original—a little over $1 million investment. They are now planning a $2.4 million expansion. And this was not possible without the use of the Enterprise Zone credits. They used $114,000 in credits.

And one other thing that—I mean, it just occurred to me yesterday. I do not know how many people are familiar with some of the background of the Enterprise Zones in the original Hong Kong model. Apparently, whether it was the British who looked at Hong Kong and they said, this is great, what is going on here economically. They have got low taxes, low wages, and low regulation. And this is what makes it an exciting entrepreneurial environment.

And I was thinking the other day—if Hong Kong had had high taxes and high wages and high regulation, would we still have a Hong Kong? Of course we would. It probably would not have the kind of environment that we are trying to create. There would not be as much done as we see today. But I think we would still have a Hong Kong.

So I do not think the fact that not everything is new is necessarily a reason not to go ahead with the program.

Senator LIEBERMAN. Let me ask you this final question, and then I will yield to Senator Boschwitz.

Has either Minnesota or Connecticut waived any environmental or health regulations or laws in the Enterprise Zone?

Mr. HELGESEN. I do not believe that we have.

Mr. JAMBOIS. No, we have not either.

Senator LIEBERMAN. I appreciate that. Senator Boschwitz.

Senator BOSCHWITZ. Where do you have your Enterprise Zones in Connecticut? How large are the zones? How much of the community do they encompass?

When we talk about Enterprise Zones, as the witnesses from Minnesota have said, we talk about some fairly small cities. The largest one was Mankato. Is the whole city of Mankato an Enterprise Zone?

Mr. HELGESEN. No. In Minnesota there is a maximum of 400 acres. In Mankato its mostly an industrial zone.

Senator BOSCHWITZ. But you said in your testimony that in Minnesota an Enterprise Zone can incorporate more than one city—400 acres?

Mr. JAMBOIS. That is correct, Senator. The zone itself is 400 acres—the area of distress, or the benefit area, is much greater than that.

The economic activity has to occur within a zone. The zone can be on several parcels, connected by a line. But the area that it serves—the benefit area is greater than that.

Senator BOSCHWITZ. And the zone does not have to be contiguous?

Mr. JAMBOIS. That is correct.

Mr. HELGESEN. If I could add to that. We have two clusterings of cities. In one of the clusters each city has 100 acres.

Senator BOSCHWITZ. That is up on the range?

Mr. HELGESEN. Yes. And I wish I had double-checked this, before I was asked the question. But I think in the other one they are allowed 800 acres. There is an exception for that particular zone.

Senator BOSCHWITZ. Tell me about yours; Mr. Heintz.

Mr. HEINTZ. Our zones, Senator Boschwitz, range in size from 125 acres, which is the smallest, to 700 acres, which is the largest. In the city of Hartford, for example, our State capital and the second largest community in the State, with a population of about 135,000, 130,000, the zone is 320 acres.

And it is a significant tract of land in an area that has been impoverished and blighted for, literally, decades.

The 10 communities are very diverse. We have the two largest cities, which are northeastern industrial urban centers, but we also have some of the smaller, more rural communities like Wyndam, which is in the northwest section of our State.

And these zones actually comprise a fairly significant amount of territory. Because in Connecticut, municipal boundaries are relatively small, with 169 municipalities in a rather small State. So the zones are a significant part of the property base in some of these towns.

Senator BOSCHWITZ. Mr. Heintz, in your testimony, you did not indicate how many people had been advantaged. In Minnesota they gave some numbers. Do you have a sense of what the numbers are?

Mr. HEINTZ. Yes. We have tabulated that there have been 6,662 new jobs created.

Senator BOSCHWITZ. How much?

Mr. HEINTZ. Six thousand six hundred and sixty two. And 6,915 jobs that have been retained in those zones. Total investment, Senator, in the zones of some $375,000 million.

Senator BOSCHWITZ. Wow. Well, we certainly have not spent that much in Minnesota. How did you come to that investment?

Mr. HEINTZ. That is the private sector investment.

Senator BOSCHWITZ. Oh, pardon me. I presumed that we had not had that large an investment either.

Mr. JAMBOIS. Senator, I am not certain we have not calculated those figures for private investment. We do not track them.

Senator BOSCHWITZ. Mr. Heintz, you have said that the Federal zone should incorporate the entirety of the State zone, and you also said that we should contract with a State agency to administer the Enterprise Zone. Let me comment on that.

We are having enough trouble getting some meaningful Enterprise Zone legislation through both houses and past the Adminis-

tration without saying that we are going to let the States do it, let the States spend our money.

It is not clear to me that it would be a practical suggestion, very frankly, to throw ourselves into the hands of the State.

I know that Mr. Jambois spoke about more than 33 rural enterprise zone designations. We will feel fortunate if we get 33. And so—maybe you can come back next year after we have 33, and then ask for 33 more.

But I am afraid that we probably cannot do it quite the way you suggest.

Mr. HEINTZ. Could I react, Senator, for a moment?

Senator BOSCHWITZ. Yes.

Mr. HEINTZ. It seems to me that in our system of federalism in which the States and Federal Government share in many responsibilities, that it is not unrealistic to suggest that the Department of Housing and Urban Development—at least have the authority to decide for ease of administration and effectiveness, to contract with a local agency, a State agency that has proven capacity.

In those States where zones have been operating well and effectively and have been—management studies and audits completed, it seems to me we could reduce the level of administrative paperwork and bureaucracy and disincentives, if the Secretary were given that discretion.

I certainly understand the Congress' concern about losing control over the program, but I would suggest as we look around the Federal register of discretionary programs, the States are operating many, many of those programs quite successively under Federal regulation and guidance.

Senator BOSCHWITZ. Well, I understand what you are driving at. I think that there would be some institutional objections to some of that down here—at least as I see it.

You spoke about Moorehead, MN, that 25 businesses have left in the 6 years since the Enterprise Zone has been established. You did not mention whether or not any had come?

Mr. HELGESEN. Yes. I was the one who used the figure of 25. We know that there are about 40 to 50 businesses that left in the year to 18 months before the program started. From the number of businesses where they have initiated recapture proceedings.

In other words, the businesses have ceased to operate in the zone, and the city of Moorehead is trying to recapture those credits. They have filed 18 of those with the State.

Senator BOSCHWITZ. Pardon me, I am sorry. Say that again, please.

Mr. HELGESEN. Sure. There have been 18 businesses in—so far, from the city of Moorehead that have ceased to operate in the zone, and the city has instigated recapture proceedings. They have tried to recapture the credits that they got.

So we know that there are 18 businesses that have left.

I do not have the figures for the 1½ years, for how many businesses have left. The local coordinator tells me that there are businesses that are moving in and moving out in its more normal inflow, but I do not have a number for the number that have come.

Senator BOSCHWITZ. In your testimony you said we should target disadvantaged residents, but you did not say how you propose to do

that. Could you verbalize briefly how one would properly, appropriately, and effectively target the disadvantaged?

Mr. JAMBOIS. It has to do, Senator and Mr. Chairman, with the types of businesses that receive credits—what kind of business they operate, and how the local coordinators negotiate the credits.

I think we have heard from——

Senator BOSCHWITZ. You mean that you negotiate the credits in each zone?

Mr. JAMBOIS. That is correct, Senator. The local—there are four ways to award credits in a zone, and it is between the local zone coordinator and the business to determine what type of credits will best meet the business needs and be within the confines of the law—State law and regulations, is—a business that is going to come in, or going to expand and create jobs that are available to disadvantaged people have a great chance of receiving Enterprise Zone credits sufficient to make that business go.

A business that would come in and create very high technology jobs that would not necessarily benefit the distressed population in the area is likely to receive significantly fewer credits.

Senator BOSCHWITZ. You said in your testimony that businesses from outside the Enterprise Zone boundaries could relocate within the zone, and this would strengthen the zone, while it would weaken the adjacent areas.

And then you said in Minnesota, "We prevent this practice." But you did not say how we prevent it?

Mr. JAMBOIS. We have an anti-pirating provision, Senator, which prohibits a business from coming in to the zone to collect the credits unless the business can demonstrate that they are going to maintain their investment in their other site outside the zone.

Senator BOSCHWITZ. Suppose they demonstrate that they are going to move out of their other zone, and go to North Dakota or South Dakota, or who knows where. But that they are not going to maintain.

Suppose they come to you and say, put us into the Enterprise Zone, or kiss us goodbye. Then what?

Mr. HELGESEN. We have had a couple of cases come up where we have had attorneys review it, and they finally decided that it has to be very clearly established and documented that the jobs are lost. Otherwise, we will not grant credits. And we have been very, very conservative in our willingness to let cities do that.

And, Senator Boschwitz, in terms of preventing a business from moving into a zone from just outside——

Senator BOSCHWITZ. Not even from just outside, but from perhaps 100 miles away.

Mr. HELGESEN. OK. Each city council has to pass a resolution. And when a business puts in an application to become an Enterprise Zone business, the city council has to pass a resolution where they make a finding that the use of credits will not have the affect of transferring jobs from one area to another.

So it is the city council that would use each individual case and makes that decision.

Senator BOSCHWITZ. It seems to me that the city council is anxious to get a business and could make those findings rather quickly and easily.

Mr. JAMBOIS. They are also subject to our approval, Senator.

Mr. BOSCHWITZ. Have either of you in conclusion made a study, or an estimate of what passage of the Federal government's Enterprise Zone legislation will do to your Enterprise Zones, how it will supplement them, and how it will improve the results in your Enterprise Zones?

Mr. JAMBOIS. We have done no formal calculations or studies of the impact, Senator.

Mr. HEINTZ. We have not yet either, Senator.

Senator BOSCHWITZ. Thanks, Mr. Chairman, and thank you.

Senator LIEBERMAN. I want to respond with a couple of questions based on what Senator Boschwitz asked earlier.

This is the Committee on Small Business, as you know. And one of the questions I have is, what the impact of the Enterprise Zone legislation, particularly the tax credits that we are talking about in S. 58 will have on small business, and in particularly, on entrepreneurship?

Looking at the array—I understand you have another chance to do a formal study of the bill, but based on your experience in Minnesota and Connecticut, and having some general knowledge of what S. 58 includes, what would you say would be the incentives that will be most important to short-term startups?

In other words, we are concerned about the long term, and I think one of the goals here is also to create, to foster some entrepreneurial spirit.

Mr. HEINTZ. I think that our experience has been that it is mostly small businesses that are attracted to invest in the zones, because you are reducing the cost of startup. You are reducing the cost of business, in a business that is precariously balanced in those early months and years on cashflows and expenses.

And in Connecticut, as I am sure is true in Minnesota, the numbers are very stark. We have over 90,000 business establishments in Connecticut—75 percent of them employ fewer than 10 people. And it is exactly those companies that we are finding attracted to the zones, because we are reducing the cost of startup. We are reducing the cost of business itself, in giving them that extra boost in the most critical time of that business life.

Senator LIEBERMAN. Are they mostly industrial, or some commercial?

Mr. HEINTZ. We have a strong mix. They are industrial, commercial. We even will provide benefits to retail, and we also provide benefits to the construction of housing in the zones.

Mr. JAMBOIS. I concur. We think that the most important incentive for small businesses in startups is to reduce their costs. And the Enterprise Zone Program, as well as all the other programs that are run by the Department of Trade and Economic Development, try to do just that.

And we have taken it a step further. Small businesses, generally, do not have a very large tax liability, or any tax liability in their first few years of startup. If, in fact, the tax liability is less than what they would receive in Enterprise Zone credits, we actually refund them. We actually give them money to reduce their cost. It is not a lot of money, and it still shows up to be less than $2,300 per job created in those zones over the life of the program.

But, reducing costs to small businesses in startup businesses is the best incentive that anyone can give them to succeed.

Senator LIEBERMAN. And both of you—this goes back to an earlier question I asked. But both of you—I have some sense of confidence that in Connecticut and Minnesota there have actually been new businesses created because of the special incentives in an Enterprise Zone.

Mr. JAMBOIS. That is correct.

Mr. HEINTZ. Absolutely.

Mr. HELGESEN. I have looked over the list in S. 58 pretty carefully, and I think you have got a very good list of benefits. You address both—reducing costs of the business, and also with helping to raise capital. That is very important for a new business.

In Minnesota we have this refundability feature, so that if a new business does not have any tax liability, they can get a check back anyway from revenue. And that has been very heavily used in Minnesota, particularly for new businesses.

We have the debt financing credits that we use, and the job credits that we allow, have been the two most heavily used types of credits in Minnesota—particularly, I am referring to the competitive zones, or the more normal type of zones.

The other thing, I notice that Dick Coudon for the American Association of Enterprise Zones is here today. Two months ago there was a conference where that question was put to a group of Enterprise Zone leaders from around the country. I do not know if Dick—I saw him earlier. I do not know if he is still here, but they did poll their own people. I do not recall the exact list, but—or what order things came out in, but many of the things in S. 58, they felt were very important.

Senator LIEBERMAN. A different kind of question to Minnesota. Senator Baucus, I think, made a good point. One-third of the—as you know, under the 1987 legislation, one-third of the zones designated, nationally, are supposed to be rural areas.

And he raised the question by coincidence, on my morning jog this morning through Rock Creek Park, I ran into a man who was in the Governor's office in Idaho. I asked him about Enterprise Zones and he seemed very skeptical about their value to rural areas because of—just the fact that Senator Baucus indicated—the effect of deregulation.

And I suppose what he meant was the difficulty of infrastructure and support of services, telecommunications, transportation and trucking, to rural areas.

Is it worth—what has been your experience in Minnesota in the rural areas where the zones have been created? Has it really been able to overcome those obstacles?

Mr. HELGESEN. Absolutely, Senator.

Mr. JAMBOIS. Absolutely. The State of Minnesota beginning in 1987 with our Rural Development Act, has targeted greater Minnesota as an area for economic development growth in a comprehensive sense.

We have had Enterprise Zones since 1983, and we have worked with community development block grants to improve economic conditions in greater Minnesota, but we began to focus on greater Minnesota. A couple of years back there was—we had a two-econo-

my State. Between cities, metropolitan areas have prospered and done very well. The rest of the state has done very poorly.

We believe we through the Enterprise Zone Program and through our experience with the Community Development Block Grant Program and State Companion Grant Programs that we can document that these programs absolutely benefit the rural parts of the State, that they had stimulated very important investment nonagricultural and sometimes agricultural investment in the rural part of the State and have created jobs and economic opportunities for the people who live there.

Mr. HELGESEN. I would like to add, some of our rural communities in Minnesota have had pretty good infrastructure, and the problem has been that the businesses have left. For example, in Key River Falls, there has not needed to be a lot of investment.

We have some other cases where communities have made the decision to take the risk of developing that infrastructure primarily because they have got an Enterprise Zone Program, and they know if they do develop the infrastructure, there is going to be some resources to help businesses start up there and expand.

So, the Enterprise Zone has been critical in helping the communities to deal with the infrastructure.

Senator LIEBERMAN. I want to thank the three of you. Your testimony has been outstanding, it has been very informed, and it will be very helpful to us as we go forward.

Senator BOSCHWITZ. I share those feelings. Without singling out the folks from Minnesota, I must say that I like the fact that you have problems, discussions, and solutions in your testimony. It was more directed and more precise than we often hear around here.

Senator LIEBERMAN. You were not bad, either.

Mr. HEINTZ. Thank you, Senator.

Senator LIEBERMAN. Thank you very much. Timing is perfect. Congresswoman Oakar just arrived, and we would invite her to offer her testimony at this time.

Thank you very much for coming over, Congresswoman. We know that you have been actively interested in Enterprise Zones and have Chaired the Committee interested in looking at them on the House side. We welcome you and look forward to your testimony at this time.

STATEMENT OF HON. MARY ROSE OAKAR, A U.S. REPRESENTATIVE FROM THE STATE OF OHIO

Ms. OAKAR. Thank you very much, Mr. Chairman and distinguished Members of the Senate Small Business Committee. I am delighted to be able to appear before you.

Senator, I would like to ask unanimous consent that my entire statement in the interest of your precious time be submitted for the record.

Senator LIEBERMAN. Without objection, we will certainly do that.

Ms. OAKAR. I appreciate the opportunity to appear before you today. It is an excellent idea that this Committee hold hearings to explore the impact of Enterprise Zones on small business opportunities.

I think the Congress has long recognized the importance of small business activity in this country through a series of actions, certainly by creating a Committee on Small Business which dates back to 1941. So, we are delighted to see that this, of course, is a major issue before this Committee.

Currently, it is believed that small businesses will play the most, in many ways, important role in the success or failure of Enterprise Zones. The 1985 study by the Small Business Administration indicated that small businesses appear to be the most important source of employment growth in Enterprise Zones. The report, which studied eight cities, evaluated Enterprise Zone impacts on business and employment growth; and in seven of the eight cities examined employment's increase in smaller establishments while it declined or stagnated in larger firms.

So, now the Congress and this Committee will address how to incorporate Federal incentives into the relatively new Federal Enterprise Zone Program if we do indeed adopt it.

As you know, Enterprise Zone legislation has been introduced in every Congress since 1980 in bipartisan spirit with Senate passage having taken place in the 98th Congress. And we in the 100th Congress established a Federal Enterprise Zone Program by authorizing under title VII of the Housing and Community Development Act of 1987 the selection of the 100 federally designated assistance areas.

And while the act which is Public Law provides for the designation of Enterprise Zones, the problem is it does not provide any Federal incentives to draw businesses to those zones, and that certainly is the area of concern.

The Subcommittee which I Chair on the House side, the Subcommittee on Economic Stabilization for the Banking, Finance, and Urban Affairs Committee, has held two hearings on this legislation.

In the first hearing we reviewed the role of Enterprise Zones as an economic development tool and whether there are other programs including the UDAG Program that could achieve desired economic results. And at that time we heard from our former colleague who is now our Secretary of HUD, Mr. Kemp.

The testimony focused on the status of applications of the zone designation. We discussed the successes and the shortcomings of Enterprise Zones in general.

The second hearing was held in the South Bronx district in respect to one of the original cosponsors of the bill, Robert Garcia of New York. At that hearing we again heard from Secretary Kemp. We also heard from New York City and State officials on the success of their opportunity zones and from business participants located in these zones.

Though we are examining a new Federal Enterprise Zone Program, I think we are able to engage the important potential impact by reviewing some of the experiences of State and local programs. Prior to Federal action in the United States more than 30 States and the District of Columbia have established these types of programs. Most States required a broad range of incentives, and I really want to stress this, a broad plate of incentives, as opposed to just one type of incentive—including tax credits, abatements, ex-

emptions, regulatory relief, grants, loans, and loan guarantees, to businesses investing in the zone.

Across the country Enterprise Zones have become a valuable economic tool in attracting new businesses to particularly those distressed areas. However, academic and urban experts have offered diverse views on the effectiveness of Enterprise Zone Programs.

A December 1988 GAO report on the Maryland Enterprise Zone experience indicated that the program did not stimulate local economic growth as measured by employment or strongly influence most employers' decisions about business location.

The GAO suggested consideration of a Federal Demonstration Program with varied incentives rather than a large-scale program.

In August 1986, HUD report on 10 State Enterprise Zones generally found that zone designation appears to produce a positive and tangible impact on business investment in the zones, and it is seen by investors as evidence of a long-term commitment to and the interest in the zone by local government.

Additionally, that report found that for some small- and medium-sized cities starting economic development programs, the Enterprise Zone designation has become an organizing mechanism for the community to assess its needs and put together a package that becomes the city's principal economic development strategy.

The hearing in New York, where zones are limited in size, it revealed that the Enterprise Zone Program has been a great success. There the State Zone Program is State assisted and locally administered, but the program's success or failure rests not only with the State's resources and the commitment of high State officials, but on the local commitment, local officials, local economic and human resource agencies, and local development agencies.

So, I think we can discern that there have been successful and unsuccessful Enterprise Zones. Currently, seven Enterprise Zone bills have been introduced in the 101st Congress.

I have certainly supported the Enterprise Zone concept, and I must say I have been one of the few Democrats initially to support it from its beginning, but I do have some concern that we not put all of our eggs in one basket. I think if you want to provide incentives to distressed areas in particular, you want to allure small businesses in particular, which this Committee certainly realizes makes up 95 percent of all the businesses in this country and employs the most people, I think we really do have to take a look at the varieties of options.

I think the Enterprise Zone legislation does not replace any other type of legislation. I am a strong supporter.

I want my distinguished Senators to know of the UDAG concept. If you take a look at the impact that it has had in my own district of Cleveland, OH, it has had a tremendous influence on small and larger businesses who otherwise would not have invested. And most importantly it has created an awful lot of jobs, and I think it is fair to say that my own home town is kind of a comeback city because of these helpful public/private partnerships. I think that is what we are talking about here.

So, I would urge the Committee to take a look at the following questions. No. 1, where will new businesses, whether small or

large, get capital for start-ups? How much money is needed for this.

No. 2, when the economy is not expanding, will the Enterprise Zone activity created be within the national economic expansion level?

No. 3, will businesses merely transfer from one location to the zone thus creating another distressed area?

No. 4, what happens to businesses already in the Enterprise Zone? Will they be driven out? Are there not equity questions if you give regulatory relief or tax relief to one business but not to the business next door or across the street?

No. 5, is it better to give tax relief at the end rather than a grant up front for start-up, and will other Federal grant programs be targeted to the Enterprise Zone?

No. 6, what kind of tax benefits are appropriate in an era of tax reform?

No. 7, if necessary, how will infrastructure improvements—and I think this is really key, particularly in older communities whether they are rural or urban—how will infrastructure improvements be financed in the Enterprise Zone to compliment whatever you do with that targeted area?

And, No. 8, what will Enterprise Zones cost? Would revenues be reduced thereby requiring enactment of other measures to increase revenues or reduce spending?

I think with careful planning I think you can discern the answers to those questions, and I honestly believe that that array of, or that option of Enterprise Zone legislation ought to be part of a plate of options you have, particularly so small businesses with the proper incentives can forge ahead and be successful and thus create new jobs and stimulate our economy.

Thank you very much. I would be delighted to answer any questions if you want, and I am very pleased that you asked me to testify.

[The prepared statement of Congresswoman Oakar follows:]

TESTIMONY OF CONGRESSWOMAN OAKAR
BEFORE THE SENATE SMALL BUSINESS COMMITTEE
ON ENTERPRISE ZONES 6/21/89

GOOD MORNING MR. CHAIRMAN AND MEMBERS OF THE SENATE SMALL BUSINESS COMMITTEE. I AM CONGRESSWOMAN MARY ROSE OAKAR AND I REPRESENT THE 20TH DISTRICT OF OHIO. CURRENTLY, I AM CHAIRWOMAN OF THE HOUSE BANKING, FINANCE, AND URBAN AFFIARS SUBCOMMITTE ON ECONOMIC STABILIZATION. DURING THE COMMITTEE ORGANIZATIONAL PROCESS THIS YEAR, THE JURISDICTION OF MY SUBCOMMITTEE WAS EXPANDED TO INCLUDE, AMONG OTHER AREAS, ENTERPRISE ZONES--WHICH HAD FORMERLY BEEN UNDER THE JURISDICTION OF THE HOUSING AND COMMUNITY DEVELOPMENT SUBCOMMITTEE.

I APPRECIATE THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY. IT IS AN EXCELLENT IDEA THAT THIS COMMITTEE IS HOLDING HEARINGS TO EXPLORE THE IMPACT OF ENTERPRISE ZONES ON SMALL BUSINESS OPPORTUNITIES. THE CONGRESS HAS LONG RECOGNIZED THE IMPORTANCE OF SMALL BUSINESS ACTIVITY IN THIS COUNTRY THROUGH A SERIES OF ACTIONS. THE HOUSE CREATED THE SELECT COMMITTEE ON SMALL BUSINESS IN 1941 AND THE SENATE FOLLOWED IN 1950. RECOGNIZING THE IMPORTANCE OF THE WORK PERFORMED, THE SENATE AND HOUSE MADE THE COMMITTEE A PERMANENT SELECT COMMITTEE IN 1968 AND 1974 RESPECTIVELY.

THE CONGRESS ALSO CREATED THE SMALL WAR PLANTS ADMINISTRATION IN WORLD WAR II AND THE SMALL DEFENSE PLANTS

ADMINISTRATION IN 1950 TO ASSURE SMALL FIRM PARTICIPATION IN MAJOR MILITARY MOBILIZATIONS. WE CREATED THE SMALL BUSINESS ADMINISTRATION IN 1953 TO EXTEND THIS INVOLVEMENT IN THE MILITARY AND CIVILIAN PROCUREMENT PROCESSES AND PROVIDE LONG TERM FINANCING TO SMALL FIRMS. LAST YEAR SBA PROVIDED $2.5 BILLION IN FEDERAL GUARANTEES FOR LOANS THAT AVERAGED NEARLY TEN YEARS IN LENGTH.

AND IN 1958, THE CONGRESS CREATED THE SMALL BUSINESS INVESTMENT COMPANY (SBIC) AND CERTIFIED DEVELOPMENT COMPANY PROGRAMS THAT RESULTED IN 300 SBICs, 100 MINORITY SBICs, AND 350 CERTIFIED DEVELOPMENT COMPANIES. TOGETHER THESE PROGRAMS PROVIDE ALMOST ONE BILLION A YEAR IN FINANCING TO RURAL AND URBAN SMALL BUSINESSES TO (1) CREATE JOB PRODUCTS, (2) TO CREATE NEW BUSINESSES AND NEW INDUSTRIES, AND (3) TO STABILIZE ECONOMIES OF URBAN AND RURAL AREAS.

SO IT IS OBVIOUS TO ME THAT THE CONGRESS, AND ESPECIALLY THE SMALL BUSINESS COMMITTEES HAVE AN EXCELLENT RECORD RECOGNIZING THAT THE NATION'S SMALL BUSINESS PEOPLE REPRESENT A VITAL SEGMENT OF OUR BUSINESS POPULATION AND OUR NATION'S STRENGTH. AND I THINK THAT IT IS APPROPRIATE AND TIMELY THAT YOU ARE NOW ADDRESSING AN ISSUE THAT MAY ENHANCE SMALL BUSINESS' ABILITY TO EXPAND.

FEW DENY THAT SMALL BUSINESS PLAYS A VITAL ROLE IN OUR ECONOMY. ACCORDING TO THE SBA, SMALL BUSINESSES, INCLUDING THE SELF-EMPLOYED ACCOUNT FOR MORE THAN HALF OF THE UNITED STATES PRIVATE SECTOR LABOR FORCE. THE SBA STATE OF SMALL BUSINESS REPORTS REFLECT THAT SMALL FIRMS CONSISTENTLY CREATE SUBSTANTIALLY MORE THAN ONE-HALF THE NEW JOBS ADDED TO THE ECONOMY, AND UP TO 80 TO 100 PERCENT DURING ECONOMIC DOWNTURNS WHEN THEY ARE NEEDED THE MOST.

CURRENTLY, IT IS BELIEVED THAT SMALL BUSINESSES WILL PLAY AN IMPORTANT ROLE IN THE SUCCESS OR FAILURE OF ENTERPRISE ZONES. A 1985 STUDY BY THE SMALL BUSINESS ADMINISTRATION (SBA) INDICATED THAT SMALL BUSINESSES APPEAR TO BE THE MOST IMPORTANT SOURCE OF EMPLOYMENT GROWTH IN ENTERPRISE ZONES. THE REPORT, WHICH STUDIED EIGHT CITIES, EVALUATED ENTERPRISE ZONE IMPACTS ON BUSINESS AND EMPLOYMENT GROWTH. IN SEVEN OF THE EIGHT CITIES EXAMINED, EMPLOYMENT INCREASED IN SMALLER EXTABLISHMENTS, WHILE IT DECLINED OR STAGNATED IN LARGER FIRMS.

SO NOW, THE CONGRESS AND THIS COMMITTEE WILL ADDRESS HOW TO INCORPORATE FEDERAL INCENTIVES INTO THE RELATIVELY NEW FEDERAL ENTERPRISE ZONE PROGRAM. AS YOU KNOW, ENTERPRISE ZONE LEGISLATION HAS BEEN INTRODUCED IN EVERY CONGRESS SINCE 1980, WITH SENATE PASSAGE HAVING TAKEN PLACE IN THE 98TH CONGRESS. THE 100TH CONGRESS ESTABLISHED A FEDERAL ENTERPRISE ZONE PROGRAM BY

AUTHORIZING, UNDER TITLE VII OF THE HOUSING AND COMMUNITY DEVELOPMENT ACT OF 1987, THE SELECTION OF 100 FEDERALLY DESIGNATED ASSISTANCE AREAS. WHILE THE ACT, WHICH IS PUBLIC LAW 100-242, PROVIDES FOR THE DESIGNATION OF ENTERPRISE ZONES, IT DOES NOT PROVIDE FEDERAL INCENTIVES TO DRAW BUSINESSES TO THE ZONES.

MY SUBCOMMITTE HAS HELD TWO HEARINGS ON ENTERPRISE ZONES. IN THE FIRST HEARING WE REVIEWED THE ROLE OF ENTERPRISE ZONES AS AN ECONOMIC DEVELOPMENT TOOL AND WHETHER THERE ARE OTHER PROGRAMS, INCLUDING THE UDAG PROGRAM, THAT COULD ACHIEVE DESIRED ECONOMIC RESULTS. AT THAT TIME WE HEARD FROM MY FORMER COLLEAGUE, WHO IS NOW THE SECRETARY OF HUD, JACK KEMP. THE TESTIMONY FOCUSED ON THE STATUS OF APPLICATIONS FOR FEDERAL ENTERPRISE ZONE DESIGNATION, AND WE DISCUSSED THE SUCCESSES AND SHORTCOMINGS OF ENTERPRISE ZONES IN GENERAL.

THE SECOND HEARING WAS HELD IN THE SOUTH BRONX DISTRICT OF MY COLLEAGUE ROBERT GARCIA, WHO IS ONE OF THE CHIEF SPONSORS OF H.R.6, THE "ENTERPRISE ZONE IMPROVEMENTS ACT OF 1989". AT THAT HEARING WE AGAIN HEARD FROM SECRETARY KEMP. WE ALSO HEARD FROM NEW YORK STATE AND CITY OFFICIALS ON THE SUCCESS OF THEIR "OPPORTUNITY ZONES" AND FROM BUSINESS PARTICIPANTS LOCATED IN THE ZONES.

THOUGH WE ARE EMBARKING ON A NEW FEDERAL ENTERPRISE ZONE PROGRAM WE MAY BE ABLE TO GUAGE THE POTENTIAL IMPACT BY REVIEWING SOME OF THE EXPERIENCES OF STATE AND LOCAL ENTERPRISE ZONE PROGRAMS. PRIOR TO FEDERAL ACTION, IN THE UNITED STATES, OVER 30 STATES AND THE DISTRICT OF COLUMBIA HAD ESTABLISHED ENTERPRISE ZONES. MOST STATES PROVIDE A BROAD RANGE OF INCENTIVES-- INCLUDING TAX CREDITS, TAX ABATEMENTS, TAX EXEMPTIONS, REGULATORY RELIEF, GRANTS, LOANS, AND LOAN GUARANTEES-- TO BUSINESSES INVESTING IN THE ZONE. ACROSS THE COUNTRY, ENTERPRISE ZONES HAVE BECOME A VALUABLE ECONOMIC TOOL IN ATTRACTING NEW BUSINESSES TO DISTRESSED AREAS. HOWEVER, ACADEMIC AND URBAN EXPERTS HAVE OFFERED DIVERSE VIEWS ON THE EFFECTIVENESS OF ENTERPRISE ZONE PROGRAMS.

A DECEMBER 1986 GAO REPORT ON THE MARYLAND ENTERPRISE ZONE EXPERIENCE INDICATED THAT THE PROGRAM DID NOT STIMULATE LOCAL ECONOMIC GROWTH AS MEASURED BY EMPLOYMENT OR STRONGLY INFLUENCE MOST EMPLOYERS' DECISIONS ABOUT BUSINESS LOCATION. THE GAO SUGGESTED CONSIDERATION OF A FEDERAL DEMONSTRATION PROGRAM WITH VARIED INCENTIVES RATHER THAN A LARGE-SCALE PROGRAM.

AN AUGUST 1986 HUD REPORT ON 10 STATE ENTERPRISE ZONES GENERALLY FOUND THAT ZONE DESIGNATION APPEARS TO PRODUCE A POSITIVE AND TANGIBLE IMPACT ON BUSINESS INVESTMENT IN THE ZONES. IT IS SEEN BY INVESTORS AS EVIDENCE OF A LONG TERM COMMITMENT TO

AND INTEREST IN THE ZONE BY LOCAL GOVERNMENT. ADDITIONALLY THE REPORT FOUND THAT FOR SOME SMALL AND MEDIUM-SIZE CITIES STARTING ECONOMIC DEVELOPMENT PROGRAMS, THE ENTERPRISE ZONE DESIGNATION HAS BECOME AN ORGANIZING MECHANISM FOR THE COMMUNITY TO ASSESS ITS NEEDS AND PUT TOGETHER A PACKAGE THAT BECOMES THE CITIES' PRINCIPAL ECONMIC DEVELOPMENT STRATEGY.

AND MY HEARING IN NEW YORK, WHERE ZONES ARE LIMITED IN SIZE, REVEALED THAT THE ENTERPRISE ZONE PROGRAM HAS BEEN A SUCCESS. THERE THE STATE ZONE PROGRAM IS STATE ASSISTED AND LOCALLY ADMINISTERED, BUT THE PROGRAM'S SUCCESS OR FAILURE RESTS NOT ONLY WITH THE STATE'S RESOURCES AND THE COMMITMENT OF HIGH STATE OFFICIALS, BUT ON LOCAL COMMITMENT, LOCAL OFFICIALS, LOCAL ECONOMIC AND HUMAN RESOURCE AGENCIES, AND LOCAL DEVELOPMENT AGENCIES.

SO WE CAN SEE THAT THERE HAVE BEEN SUCCESSFUL AND UNSUCCESSFUL ENTERPRISE ZONES. CURRENTLY, SEVEN ENTERPRISE ZONE BILLS HAVE BEEN INTRODUCED IN THE 101ST CONGRESS. I HAVE SUPPORTED THE ENTERPRISE ZONE CONCEPT SINCE IT WAS FIRST INTRODUCED. I AM NOW A CO-SPONSOR OF H.R.6, THE RANGEL-GARCIA ENTERPRISE ZONE BILL. BUT I MUST SAY, I HAVE SOME CONCERN ON THE ENTERPRISE ZONE CONCEPT THAT WE NOT "PUT ALL OF OUR EGGS IN ONE BASKET". THERE ARE OTHER ECONOMIC DEVELOPMENT TOOLS THAT HAVE A PROVEN TRACK RECORD IN PROMOTING ENTREPRENEURSHIP,

INVESTMENT, DEVELOPMENT AND JOBS IN DISTRESSED AREAS. I HAVE NO DOUBT THAT ENTERPRISE ZONES WILL BE IMPORTANT IN FIGHTING POCKETS OF POVERTY AND URBAN AND RURAL BLIGHT. BUT I BELIEVE THAT ENTERPRISE ZONES ARE JUST PART OF THE ANSWER FOR REVIVING AN ECONOMY. LIKE OTHER DEVELOPMENT TOOLS, IT HAS A BETTER CHANCE OF SUCCESS WHEN IT IS PART OF A COMPREHENSIVE DEVELOPMENT PLAN.

AND MY HEARINGS REVEAL THAT THERE ARE SOME QUESTIONS THAT STILL NEED TO BE ANSWERED:

1. WHERE WILL NEW BUSINESSES, WHETHER SMALL OR LARGE, GET CAPITAL FOR START UPS? HOW MUCH MONEY IS NEEDED FOR THIS?

2. WHEN THE ECONOMY IS NOT EXPANDING, WILL THE ENTERPRISE ZONE ACTIVITY CREATED BE WITHIN THE NATIONAL ECONOMIC EXPANSION LEVEL?

3. WILL BUSINESSES MERELY TRANSFER FROM ONE LOCATION TO THE ZONE, THUS CREATING ANOTHER DISTRESSED AREA?

4. WHAT HAPPENS TO BUSINESSES ALREADY IN THE ENTERPRISE ZONE? WILL THEY BE DRIVEN OUT? ARE THERE NOT EQUITY QUESTIONS IF YOU GIVE REGULATORY RELIEF OR TAX RELIEF TO ONE BUSINESS, BUT NOT TO THE BUSINESS NEXT DOOR OR ACROSS THE STREET?

5. IS IT BETTER TO GIVE TAX RELIEF AT THE END RATHER THAN A GRANT UP FRONT? WILL OTHER FEDERAL GRANT PROGRAMS BE TARGETTED TO THE ENTERPRISE ZONE?

6. WHAT KIND OF TAX BENEFITS ARE APPROPRIATE IN AN ERA OF "TAX REFORM"?

7. IF NECESSARY, HOW WILL INFRASTRUCTURE IMPROVEMENTS BE FINANCED IN THE ENTERPRISE ZONE?

8. WHAT WILL ENTERPRISE ZONES COST? WOULD REVENUES BE REDUCED THEREBY REQUIRING ENACTMENT OF OTHER MEASURES TO INCREASE REVENUES OR REDUCE SPENDING?

THESE ARE JUST A FEW OF THE QUESTIONS THAT HAVE TO BE ANSWERED. I HAVE BEEN ONE OF THE FEW DEMOCRATS TO CONSISTENTLY SUPPORT THE CREATION OF THE ENTERPRISE ZONE TO STIMULATE THE RE-SETTLEMENT OF DISTRESSED AREAS. I AM KEEPING AN OPEN MIND ON THE ISSUE AND I DO PLAN TO HOLD ADDITIONAL HEARINGS IN MY SUBCOMMITTEE TO ADDRESS THESE AND OTHER QUESTIONS.

AGAIN, I APPRECIATE THE OPPORTUNITY TO TESTIFY BEFORE YOU TODAY. UNFORTUNATELY, MY SCHEDULE DOES NOT ALLOW ME TO ANSWER YOUR QUESTIONS TODAY; BUT I WOULD BE MORE THAN HAPPY TO HAVE YOU SUBMIT QUESTIONS TO ME AND I WILL ANSWER THEM FOR THE RECORD. THANK YOU.

Senator LIEBERMAN. Thank you very much, Congresswoman. I know you are in a hurry, and I want to particularly thank you for the questions you posed at the end. I think they are very strong points to make that this Enterprise Zone idea should not be seen as the answer, but it is part of a package of governmental support and enticement to create a good public/private partnership.

Let me ask you what is frankly a political question which is what is your estimate of how this legislation is doing on the House side?

Ms. OAKAR. Well, we have a number of co-sponsors, Senator, on both sides of the aisle, and it is interesting to me that in the initial speech that our former Speaker gave, he mentioned that as part of his legislative priorities.

We have had two hearings in my Subcommittee that has jurisdiction over it, and other grants programs. And once we finish with the Defense Production Act, which we obviously have jurisdiction over, I am going to try to mark-up the bill and bring it to the Full Committee, and hopefully the Ways and Means Committee then will take that certain initiative.

I think the fact that Charlie Rangel on the Ways and Means Committee is one of the major sponsors this time gives a good signal.

Senator LIEBERMAN. That is encouraging.

Senator Boschwitz.

Senator BOSCHWITZ. No, I have no questions. I understood that Mrs. Oakar has some scheduling demands that require her to move on.

Senator LIEBERMAN. Thank you. For our part we certainly look forward to working with you. You have been a leader in this for a long time, and I hope we can bring it to a successful conclusion in this Congress.

Ms. OAKAR. I thank you, and I just wanted to add, Senators, that I think you have—I have always felt that the Small Business Committees—and I am not a Member of the one on the House side—but I really think the potential of this Committee in creativity and in discussing new avenues of opportunities and incentives for our businesses is just a wonderful opportunity.

We are sort of at a crossroads in terms of new ideas, and so I certainly look forward to working with both of you and Members of this distinguished Committee.

Senator LIEBERMAN. Thank you. That is just what we are trying to do today. Good day to you.

Let me now call the panel of local administrators, Iric Nathanson, Beverly Dawes, and William Ginsberg. We welcome all three of you. You are the folks out in the field who have to live with the ideas and policies that are implemented that are adopted in Washington and your State capitals and make them all work. So, we particularly look forward to your testimony.

I note in the order of listing of the witnesses in a spirit of magnanimity that the gentleman from Minnesota is listed first, so I would call on him and then go to Ms. Dawes and then to Mr. Ginsberg.

STATEMENT OF IRIC NATHANSON, FINANCE COORDINATOR, MINNEAPOLIS COMMUNITY DEVELOPMENT AGENCY, MINNEAPOLIS, MN

Mr. NATHANSON. My name is Iric Nathanson, and I am the finance coordinator for the Minneapolis Community Development Agency. The City of Minneapolis is an administrator of the State program that you heard described in the earlier panel.

We administer a 400-acre zone under the competitive phase of the program, and I would like to share with you some of our numbers so you get a sense of the quantitative impact of the program.

Senator BOSCHWITZ. Where is it, just for my edification? I am not quite sure where it is physically located.

Mr. NATHANSON. Senator, the zone is not a contiguous area. There are pieces of our Enterprise Zone in the Near North Side, in the Franklin Avenue area, the Philips neighborhood, and the Lake Street area. There are small pockets of distress throughout the inner tier neighborhoods of Minneapolis.

Senator BOSCHWITZ. And St. Paul?

Mr. NATHANSON. St. Paul has a similar program. I am not familiar with their specific geography.

Since the start of the program in 1985 the city of Minneapolis has allocated over $3.5 million and State credits to 17 local firms. These firms have invested over $60 million in capital improvements, in the city's target areas. They have retained a total of 328 jobs and are creating an additional 852 jobs.

Based on our analysis we know that the State Enterprise Zone has done much to help facilitate this investment and job creation. But I use the term "help facilitate" because it would be an overstatement to say that the Enterprise Zones in and of themselves have generated this activity.

The Enterprise Zone is a key factor, but it is only one factor.

In Minneapolis the program is very important in terms of job retention. A Minneapolis firm can only obtain the credits if it is already located in the city of Minneapolis. In other words, we cannot use the program to attract a company from St. Paul to move into Minneapolis. For a firm that is contemplating an expansion, we are able to use the Enterprise Zone to keep that firm in Minneapolis. We can move them into a target area rather than have them move out to a third tier suburb.

We have a core with problems, surrounded by a suburban area that is healthy and thriving. And our effort is to try to divert some of that investment into our target areas.

In Minneapolis we have a strong tradition of public/private partnerships, and those partnerships provide the foundation for our revitalization efforts.

The partnerships involve Government and business, but they also include the affected communities. That is a key issue for us in Minneapolis. The Enterprise Zone after all is not just a matter of providing tax credits for business development. It is also a mechanism to revitalize our distressed communities. And if we are to revitalize those communities, we need to encourage their direct participation in the process.

I can give you some concrete examples of how this would relate to the Enterprise Zone designation process. Minneapolis, our inner city communities have established a series of job banks where local community residents set up an employment referral system, locate their neighbors who are in need of jobs link those neighbors with businesses that need employees.

The Enterprise Zone Program anticipates that businesses will be hiring from the neighborhoods but without a mechanism like NET, the Neighborhood Employment Network that funnels neighborhood residents to target area businesses. There is no guarantee that that link will be made.

A NET does a lot to provide entry level jobs for target area residents, and we recognize that we need more than entry level jobs. We also need career ladders so entry level workers can move up to higher paying jobs. One of the new things we are doing now is developing a program where businesses will bring in entry level workers, and help train those workers.

Under this project, target area residents can get a $4.50 an hour entry level job. They can work up after some training into a career ladder, with a possibility of maybe we will have the option of making $12 to $13 an hour, which is really a family support wage.

We have just done this on a pilot project with automated machine tool operators. We are hoping to expand this concept to other employment sectors.

The ladder project is one way that communities can participate in the revitalization process. We would urge that the Enterprise Zone designation process include a provision for bonus points for local communities that can devise creative ways of involving their communities in the revitalization process.

I would like to make three specific proposals related to S. 58 before I close. First, local communities should have a role in designating Enterprise Zone businesses so that the Enterprise Zone process can be linked to the full array of other revitalization efforts.

Disadvantaged worker credit should be modified. Under S. 58, a business can get a credit for employing a worker who is considered to be economically disadvantaged, but S. 58 defines an economically disadvantaged individual as someone whose family income does not exceed AFDC grant level plus the value of foodstamps for that family.

In Minneapolis that would mean that only a family that has an income of about $660 a month would be eligible for this credit. That is a wage of $3.87 an hour, which is slightly higher than the existing minimum wage, but below the new minimum wage advocated by the Bush Administration. What this means is that under S. 58, only workers who are employed at minimum wage or subminimum wage levels will be eligible for the disadvantaged credit.

What we propose is that rather than qualify the disadvantaged worker based on his current income that we qualify him based on his income during the previous year. So that if he was at poverty level the year before but was able to move into a career level job, that he would be able to qualify the credit.

And finally, we would propose some revisions to the Enterprise Zone eligibility process so that industrial areas located adjacent to

distressed areas qualify for Enterprise Zones. Under the existing designation system in the 1987 act, only neighborhoods that have a high level of poverty and unemployment can be qualified for Enterprise Zones. Under the 1987 act, only residential areas are qualified for Enterprise Zone designation. And if you have a deteriorating industrial neighborhood next to a low income area, that deteriorating industrial area is not eligible, because there is not sufficient population that is going to meet the distressed criteria.

That concludes my testimony. I will be glad to answer questions.

[The prepared statement of Mr. Nathanson follows:]

Testimony of Iric Nathanson
to the Senate Committee on Small Business
June 21, 1989
Washington, D. C.

Mr. Chairman, Members of the Committee. I appreciate the opportunity to appear before you today for this hearing on enterprise zones. My name is Iric Nathanson and I am the Finance Coordinator at the Minneapolis Community Development Agency.

I am here to discuss Minneapolis' experience with the State of Minnesota's Enterprise Zone and to comment on the implications of our local experience for a federal enterprise zone program. I also intend to discuss several proposals developed by our Agency to modify pending federal enterprise zone legislation. I am pleased to note that Senator Boschwitz, the ranking minority member of this Committee, is a chief sponsor of S 58, the Enterprise Zone Improvements Act of 1989.

The City of Minneapolis is a participant in the Competitive Cities component of the State Enterprise Zone Program, established by the Minnesota Legislature in 1983.

Under the State Program, Minneapolis allocates state and local tax credits to new or expanding businesses located in a 400 acre zone established by the Minneapolis City Council.

Businesses located in the Zone are eligible to receive four kinds of credits:

1. An exemption from state sales taxes for the purchase of construction materials or equipment.
2. A credit against the employers income tax for new permanent workers employed in the Zone.
3. An income tax credit for a percentage of the cost of debt financing used to construct new facilities or expand or rehabilitate existing facilities.
4. A local property tax credit, funded by the State of Minnesota, for a portion of the property taxes paid by a new facility or an expansion of an existing facility.

The aim of this program is generate new economic growth and job creation in our City's Enterprise Zone which includes portions of seven inner-tier neighborhoods. In Minneapolis, the program is designed to complement on-going redevelopment activities aimed at stimulating private commercial and industrial development. A key focus of the Program is the creation of job opportunities for low income City residents.

The Minneapolis City Council has directed the Minneapolis Community Development Agency to administer the Enterprise Zone Program. Our staff responsibilities include marketing the Program to prospective participants, analyzing requests from businesses for tax credit allocations and transmitting Enterprise Zone applications to the City Council for its review and approval.

In Minnesota, eligibility for Zone credits parallels the eligibility for Industrial Revenue Bond (IRB) financing. Several businesses uses are prohibited from obtaining Zone credits and IRB financing. They include retail food and beverage services, properties used for the operation of financial

institutions and all recreational and entertainment facilities. Applicants for Zone credits must comply with certain program requirements. They must provide a ratio of private investment to tax credits of at least 4:1, and they must create or retain one job for every $10,000 in credits received.

Since the inception of the State Program in 1985, the City of Minneapolis has allocated over $3.5 million in credits to 17 local firms. These firms have invested over $60 million in capital improvements in the City's target areas. The 17 firms have retained a total of 328 jobs and are creating an additional 852 jobs.

Based on our analysis of these projects, we know that State Enterprise Zone credits have done much to facilitate this capital expansion and job creation. But we must note that the credits are part of a broader package of assistance that the City provides to participating businesses. That package can include industrial bond financing, assistance with land purchase and site preparation and the improvement of public infrastructure such as roads and sewers.

In Minneapolis, Enterprise Zone credits have been used effectively to retain businesses that might otherwise move out of the City. Business retention is an increasingly important economic goal for the City of Minneapolis, and it is a key element in the City's Jobs and Light Industrial Policy, adopted by the City Council earlier this year.

Enterprise Zone credits allocated by the City of Minneapolis are only available to businesses already located in the City or relocating from another

state. Because of the anti-pirating provision in the Minnesota program, the Zone credits are a key incentive for Minneapolis firms that are contemplating a move to another location in Minnesota. Other communities in Minnesota can offer much of the same financial assistance available from the City's economic development programs. But Enterprise Zone credits are the one incentive that a Minneapolis-based firm can not receive from another community in Minnesota.

The Committee has asked us to provide case histories of Enterprise Zone projects in Minneapolis. Canton North America provides a good example. Canton manufacturers high technology amplification systems for export to Europe under a licensing agreement with a German firm. The Minneapolis-based company purchased the building it now occupies in the City's Technology Corridor for use as a warehouse in 1985. In mid-1986, the Company decided to renovate the building. It was gutted and a new 18,000 square foot office, research and manufacturing facility was built in its shell. In addition to a $1 million expenditure for building renovation, Canton spent $750,000 for new production equipment. For its $1.75 million investment and for the 26 new jobs it expects to create over the next three years, Canton is receiving $173,000 in tax credits.

The Enterprise Zone Program has played an important role in encouraging Canton North America to expand its operation in Minneapolis, but its only one factor among many that has influenced this firm's capital expenditure decisions.

Based on materials developed by the National Council for Urban Economic Development (CUED) we know that businesses nationally consider a broad range of issues when they are making locational decisions. Access to markets and access to suppliers are two major factors. The availability of a skilled labor force is at the top of the list for many firms.

In Minneapolis, we are attempting to link target area revitalization with business needs for skilled labor through an innovative program operated by a local non-profit community organization, Seward Redesign. The non-profit group is working to develop career ladders for unemployed and under-employed target area residents. Companies in target areas commit to hire area residents at entry level jobs that may pay $4.50 to $5.00 an hour. These new employees are trained on the job and at night at the Minneapolis Technical Institute. After they complete their training the employer agrees to move them into career ladder jobs that can pay up to $12 or $13 an hour. Seward Redesign has just completed a successful first phase of the program for automated machine tool operators and it intends to broaden the program this summer.

In an effort to link unemployed target area residents with target area businesses, a group of community organizations has created a program known as the Neighborhood Employment Network (NET) which provides community-based job banks in seven of the City's inner-tier communities.

NETs link unemployed residents with nearby business that are seeking employees. Businesses that participate in the City's small business loan programs agree to obtain referrals from NET for their new jobs.

In Minneapolis, we are also dealing with another business development issue; the capital gap facing very small firms in target areas. We have found that young growing businesses often have difficulty obtaining bank financing because their loan requests are too small to be handled by private lenders on a cost-effective basis. Often these small businesses may need only $10,000 or $20,000 during their early years to purchase inventory or equipment. Because the commercial lending process involves intensive involvement by a commercial lending officer who monitors financial reports and makes site visits to the business, the larger financial institutions have found that it does not pay them to process these small loans. We hope to overcome this financing hurdle through a cooperative effort between private lenders and the local non-profit community development corporations. The CDCs will provide the technical assistance and monitoring usually provided by a commercial lender, and the banks will provide financing on a streamlined basis through their consumer lending systems.

The common thread that links the Career Ladder Program, the Neighborhood Employment Network and the Business Lending Project is active involvement of community-based non-profit organizations. In Minneapolis, we are convinced that active community involvement is essential part of any successful revitalization effort.

As Congress and the Administration move ahead in developing a federal enterprise zone program, I would urge you to build in a role for community organizations. Title VII of the 1987 Housing Act, which sets up a federal enterprise zone designation process, asks local applicants to describe their

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linkages with community organizations. Any new legislation should build on that foundation by providing bonus points in a application rating system for local communities that are able to demonstate new and innovative approaches for drawing their target area neighborhoods into the Enterprise Zone revitalization process.

Before closing, I would like to comment briefly on proposals developed by the Minneapolis Community Development Agency to modify Senator Boschwitz Bill, S 58, the Enterprise Zone Improvements Act of 1989.

First, local governments should certify that target area businesses qualify for federal credits. This certification process will enable local governments to coordinate enterprise zone development with other local job training, employment, and development initiatives.

Second, the definition of an "economically disadvantaged" workers should be revised. Under S 58, a business can obtain a tax credit for a worker who is considered to be "economically disadvantaged." S 58 defines "economically disadvantaged" as an individual whose family income does not exceed the AFDC grant level plus the value of food stamps for an AFDC family. In Minneapolis, that would mean a typical family income of about $665 per month or $3.87 per hour, a wage level slightly higher than the existing federal minimum but significantly below the $4.25 minimum wage advocated by the Bush Administration.

If employee tax credits in Minnesota were limited to workers whose families earned less than $665 a month, only minimum or sub-minimum wage workers at Zone businesses would be eligible for the credit. We propose that workers receive tax credit eligibility if they were low income during the year prior to gaining employment at an Enterprise Zone firm. We define "low income" to mean workers who received medical assistance, food stamps, or AFDC during the previous year or who qualified for earned income credit for low income workers during the previous year. Under our proposal, businesses would have incentive to provide career ladders for low-income workers so these workers could obtain family support wages.

Third, the waiting period for tax credit eligibility should be modified to include the time spend in job training. In S 58, a zone business must employ a economically disadvantaged worker for at least 270 days before the business can claim the job credit for that worker. Under our proposal, the time a worker spent in a training program could count towards the 270 days if the business committed to hire workers who completed the training. This proposal would provide an incentive to link enterprise zone development with job training programs for disadvantaged workers.

Fourth, the Enterprise Zone eligibility requirements should be revised. Under Title VII of the 1987 Act, Enterprise Zones must be composed of census tracts that meet certain poverty, unemployment and population decline standards. We are proposing to permit cities to include industrial areas adjacent to these tracts in their Zones if the Cities can demonstrate that development in the adjacent areas can directly benefit target area residents.. These industrial areas, which are often in need of revitalization, are currently excluded from

the consideration for Enterprise Zone designation because they don't have sufficient population to meet the enterprise zone distress standards. The current designation process limits enterprise zones, by and large, to residential areas, that may not have land available for industrial expansion.

Fifth, the 5% employee credit should be refundable. Under S 58, economically disadvantaged workers can obtain a personal tax credit equal to 5% of their income. This credit may be of no practical value to the workers because their income will be so low that they will have virtually no tax liability. By making the 5% credit refundable, low income workers could obtain tangible benefits from the credit.

Sixth, the existing child care credit in the Internal Revenue Code should be made refundable for workers in designated zone business. This provision would extend the benefits of the existing child care credit to low income workers in zone business who may have little or no tax liability.

This concludes my testimony. I would be happy to respond to questions from Committee members.

Senator LIEBERMAN. Thank you, Mr. Nathanson.

Senator Boschwitz, I want to inform you that neither of these next two witnesses has ever worked for me. Nonetheless, they are outstanding public servants, and I am glad to welcome them.

Senator BOSCHWITZ. Where are they from?

Senator LIEBERMAN. Well, they happen to be from Hartford and New Haven, CT.

Picking up on something that Mr. Nathanson said, Ms. Dawes, I understand and I know that you have done an outstanding job in that critical component of building broader community awareness of the Enterprise Zone and support for what you are trying to do, and I look forward to hearing from you about your experience.

STATEMENT OF BEVERLEY MARSHALL DAWES, MANAGER, HARTFORD ENTERPRISE ZONE, HARTFORD, CT

Ms. DAWES. Thank you. Good morning, Chairman Lieberman and Chairman Boschwitz.

I am really pleased to be here to talk about the continuing economic development of the north end community known as the Hartford Enterprise Zone. First, I would like to describe the community.

It is predominantly a minority community, 6,500 people, 320 acres. The Hartford zone is the most distressed and the most residential of all of the 10 zones in the State of Connecticut. Severity of distress was a major consideration in selection of this area. However, this particular area also offers a great deal of development potential.

First of all, it borders two high growth districts, the downtown Hartford area, as well as the North Meadows. It offers easy access to the major interstates. There is some degree of available land and buildings for commercial and industrial use. And although the zone is primarily residential, there are two major thoroughfares for commercial use that define the area.

Now, as you know, there are a variety of tools that can be used to revitalize a distressed area. In 1982 the city of Hartford decided that Enterprise Zone legislation would be one of the major tools utilized in economic development of this particular neighborhood.

Incentives include tax abatements, financing, and job grants. A complete list of the incentives is in the written testimony.

Now, as you look at the incentives and you consider the type of neighborhood that we are talking about, realistically can the offering of these incentives outweigh the liabilities, either real or perceived, associated with investing in this type of community? And also, how does one really implement a program that is going to establish the mutual benefit between private enterprise and residents?

A bit about the program and implementation. In 1985 the city of Hartford established an Enterprise Zone Office. Staffing consists of three full-time employees. In addtion, a consultant provides technical assistance to prospective zone businesses and existing zone businesses. The Enterprise Zone Office markets the Enterprise Zone, it serves as a clearinghouse for zone activity, and it promotes the

partnership between the community, the public sector, and the private sector that facilitates business growth.

Now, because of the wide array of socioeconomic problems that are plaguing this neighborhood, the existing level of incentives, alone, cannot overcome barriers to development. For this reason, in the Hartford zone we have recently begun to adopt a holistic approach, utilizing the triangular partnership and Enterprise Zone incentives. This holistic approach means a complete assessment of the needs of both the businesses and the residents, and then developing resources to address these needs.

Now I will state some of the needs that have been identified through the assessment: Job training, daycare, and other programs that will help residents gain employment, procurement assistance to businesses—of course, as businesses are able to obtain contracts, there is a likelihood of new jobs; physical improvements to the area; and programs to better the lives of residents in the area, particularly the public housing population.

A current effort to address these and other needs of the community is through a pilot program initiated by State Senator Barrows and Commissioner Heintz. A task force with representation from the Greater Hartford Chamber of Commerce, the Hartford Enterprise Zone Business Association, the Hartford Housing Authority, and various city and state departments involved in employment, financing, housing, has formed to develop and implement creative solutions to problems that are plaguing the area. We expect that this will be a model program.

A very common question: What has been our success since 1982? First of all, let me tell you that the program in Hartford focuses on job creation through the growth of existing businesses, as well as encouraging startup operations in the zone. Statistics: $30 million in new investment—that is commercial and residential investment; 1,300 jobs, new and retained jobs; 93 commercial projects, new businesses and expansions.

Now, let me cite a variety of reasons for this business activity. The most common are the availability of the Enterprise Zone incentives, along with programs such as procurement assistance to businesses being developed through the partnership effort; the labor market, a very strong consideration; and the location of the zone.

The challenge, the major challenge that remains is the challenge of offering strong Federal incentives to further encourage private investments, and to further encourage the employment and retention of residents in positions that offer advancement opportunity.

In conclusion, I would like to state that from our experience, Enterprise Zone designation, in and of itself, generate positive attention to a community that would be otherwise ignored. Rather than continued decline, Enterprise Zone incentives, in the context of a holistic approach to problems, stimulates reinvestment.

In our situation, when a business establishes and grows in a community such as the Hartford Enterprise Zone, jobs are created in areas where they are most needed.

Thank you very much. I would be glad to answer any questions that you have.

[The prepared statement of Ms. Dawes follows:]

TESTIMONY FOR HEARING
ENTERPRISE ZONES
JUNE 21, 1989

Good morning Chairman Lieberman, Chairman Boshowitz and committee members. I m Beverley Marshall Dawes, manager of the Hartford Enterprise Zone, Hartford Connecticut. I am pleased to address the US Senate Small Business Committee this morning on the continuing economic development of a community in the northend of Hartford, the Hartford Enterprise Zone.

First I'd like to describe this community. The Hartford Enterprise Zone, a predominantly black and hispanic community, consists of 320 acres. Of the 10 zones in the state of Connecticut, it is the most residential and carries the distinction of being the most distressed. To a large degree this is due to the presence of 2 large public housing projects in the community.

From the 1980 census we know the following:

(1) 52% of the population live below the poverty line as compared to 25% of the city population. Only 4% of the suburban population surrounding Hartford live below the poverty line.

(2) Per capita income is less than half of that in Hartford - $2571 in the zone, $5559 city wide.

(3) Of those 16 and older, 57% are out of the labor force as compared to 40 % in the city.

(4) Unemployment is 17% zone; 7% in the city at large.

Severity of distress was a major consideration in the selection of this community for enterprise zone designation ;however, the area also offers potential for development.

Here are some reasons:

(1) The zone is adjacent to 2 high growth business districts: the central business district and the North Meadows, an Industrial Business Development district; and there is easy access to the major interstates. A March '88 article in a local paper stated that "recent development pressure from Downtown and the North Meadows plus highway improvements make the zone desirable real estate for new zone projects."

(2) Although the zone is largely residential, there are 2 commercial/industrial thoroughfares that define the community.

(3) There is some availability of land and buildings for commercial and industrial development.

There are a variety of tools that can be used to accomplish the economic development of a community. In 1982, the City of Hartford decided that enterprise zone legislation would be one of the major tools used to revitalize this northend community. This was done in anticipation of future federal incentives that would supplement the city and state program.

Incentives include financing for small businesses and a tax abatement on real and personal tax for manufacturers and certain service sector employers. Also available is a tax deferral program for retail/commercial businesses and residential property owners. A complete listing of incentives is in Appendix A.

Realistically, can these enterprise zone incentives, solely, outweigh the liabilities (be they real or perceived) associated with investing in this community? How does one implement a program that establishes the mutual benefit between private enterprise and the community?

In 1985, the city of Hartford established an Enterprise Zone Office to market the Enterprise Zone, serve as a clearinghouse for zone activity and promote a the public/private/community partnership that will facilitate business growth. Office staff consists of 3 full-time employees. In addition, a consultant provides part-time technical assistance to prospective zone businesses and existing zone businesses. This office was established 2 1/2 years following a review of results that indicated substantial residential development, but limited business activity and job creation.

With the array of socio-economic problems plaguing this community the existing level of incentives, alone, cannot overcome barriers to development. As a result, in Hartford's zone we have recently begun to adopt a "holistic" approach to economic development, utilizing the triangular partnership and enterprise zone incentives. This approach means a complete assessment of the needs of businesses and residents and then developing appropriate resources.

Major needs include:

(1) new programs and a targeting of existing programs that will result in increased employment of residents. This encompasses job placement, job training subsidies, day care, etc.

(2) stronger incentives to attract labor intensive businesses to the zone

(3) easier access to capital

(4) procurement assistance to zone businesses

(5) increased security

(6) physical improvements

(7) programs to increase the quality of life for residents (particularly those in public housing)

A current effort to address these needs is through a pilot program initiated by state Senator Barrows and Commissioner Heintz. The goal is to develop and implement creative public/private/community solutions to problems that limit the success of Hartford's Enterprise Zone. Task force participation includes the Greater Hartford Chamber of Commerce; the Hartford Housing Authority; the Hartford Enterprise Zone Business Association; various state and city departments that represent employment and training, income maintenance, human resources, financing; and the Connecticut Small Business Development Center.

A common question - What have been our successes since 1982? Within the Hartford Enterprise Zone commercial, space for development is at a premium therefore, the program focuses on job creation through the growth of existing businesses as well as encouraging start-up operations.

During the past 7 years, there has been $30 million in new investment in the area, 1337 jobs (new and retained) and 93 commercial projects (new businesses and expansions). Examples are: A T Foote Woodworking, a zone business that purchased adjoining property to accommodate business growth; Regal Windows, a start-up manufacturer that opened the doors with 25 and projects doubling its workforce in 1 year; and Ehrlich Interiors, a 85 year-old, highly respected reupholstering company that renovated a 40,000 square foot building to meet expansion needs. Also, developers have recently broken ground for a 7 acre office/industrial park.

As to the rationale for business activity, owners have cited reasons such as the availability of enterprise zone incentives, along with programs such as procurement assistance (developed through the public/private partnership; labor market, a very strong consideration; and proximity to downtown Hartford and the major interstates. Since a major goal of the Enterprise Zone Program is to increase employment opportunities for disadvantaged residents, we capitalize on prospective zone employer interest in the zone labor pool. However, there still remains a major challenge - offering stronger legislated incentives to further encourage investment, and to further encourage the employment and retention of residents. In the interim, regarding employment, the city of Hartford has made a commitment to the Enterprise Zone Program by recruiting a zone job developer.

In conclusion, it is clear that enterprise zone designation, in and of itself, generates positive attention to a community that would otherwise be ignored. Rather than continued decline, enterprise zone incentives, in the context of a holistic approach to problems, stimulate reinvestment in economically depressed communities. When a business establishes and grows in a community such as the Hartford Enterprise Zone, job opportunities are developed where they are needed most.

Senator LIEBERMAN. Thank you very much. That was very helpful testimony, and I look forward to questioning you.

Will Ginsberg is the next witness. I know Will because he is from my hometown, or he has moved to my hometown. Anyway, he was, prior to heading Science Park Development Corporation, the Development Administrator of the city of New Haven. So he brings a unique perspective to the table, and I suppose in part can help us compare the Enterprise Zone incentives that we are talking about here with other federally sponsored development programs.

Science Park, Senator Boschwitz, is an unusual, we think, attempt to try to do something for development in an inner city neighborhood. And I welcome you, Will, and look forward to your testimony.

Senator BOSCHWITZ. Science Park is the Enterprise Zone, I gather?

Mr. GINSBERG. It is within the Enterprise Zone, yes.

STATEMENT OF WILLIAM W. GINSBERG, PRESIDENT, SCIENCE PARK DEVELOPMENT CORP., NEW HAVEN, CT

Mr. GINSBERG. Good morning, Senator Lieberman and Senator Boschwitz. I am deeply appreciative of this opportunity to appear before you on this issue this morning, and I commend each of you for the leadership you have taken on the Enterprise Zone issue, both in sponsoring these hearings and in sponsoring the legislation.

I am president of Science Park Development Corp. We are a not-for-profit corporation which is developing an 80-acre, formerly abandoned industrial site in inner city New Haven into a high technology business and research park for small businesses. Our site is within, Senator Boschwitz, within one of Connecticut's existing and one of the original Enterprise Zones in the State of Connecticut, and we are also partially within the proposed zone, New Haven, the application for which is currently pending at the Department of Housing and Urban Development. That was submitted by the city of New Haven and the State of Connecticut jointly.

Senator BOSCHWITZ. Is it flat, or are there buildings on it?

Mr. GINSBERG. Many buildings, Senator. It is a site, historic industrial site. It was once, and still is actually, the home of a much reduced operation for the manufacture of Winchester Rifles. Most of the site is abandoned at this point, but it is still populated by a number of old buildings which date from the mid-19th century up to the mid-20th century in vintage.

I believe that the Enterprise Zone Program, properly conceived, could be a potent tool to help comprehensively address the issues of urban America, because it can both help to build new economy for economically ravaged economies in our cities, and it can help to assure that the economic benefits which result are located and remain in those inner city communities.

This dual role is precisely what we are trying to do at Science Park. We are creating a new economy through technology business development. We are attempting to find ways to benefit the inner city communities from the positive economic change that comes from that kind of new economy. We are, in essence, trying to deal

with the issue of poverty which Senator Lieberman mentioned in his opening remarks.

Our industrial facilities on Winchester Avenue in New Haven epitomize the difficulty which manufacturers in cities like New Haven have faced in competing with domestic and with foreign competition. This inability to compete led to an economic decline in the heart of New Haven of such severity that the working population at our facilities fell from a peak of over 20,000 during World War II to under 1,000 by the time Science Park was created in 1981.

The Science Park strategy has been to create fundamental change in that cycle of economic decline, to create a new competitive economy through promoting innovation, and to promote innovation through the application of technology in the small business sector. Technology business has been attracted to our location, which is immediately adjacent to Yale University, which is one of the great research universities in the world.

The Science Park story demonstrates that through creation of a new economic base of applied technology, jobs can be created, private business institutions can be attracted, community institutions can be strengthened, and economic change can be made to work directly for the benefit of inner city neighborhoods.

Today, Science Park is a community of over 100 small technology companies. The project has begun, as I said, to reverse the fundamental cycle of economic decline. In an area characterized by two generations of disinvestment, over $46 million has been invested since 1982, and in an area characterized by two generations of steady loss in jobs, well in excess of 1,000 jobs have been created or retained during that time period.

The community renewal which I have referenced, which we think is an indispensable companion to economic development, is also occurring. In addition to the job creation, over 1,000 persons have received forms of job training in Science Park in recent years. Science Park has also created important partnerships with local community-based organizations to promote housing and community development in the surrounding neighborhoods. And housing and various kinds of community development, commercial development, and the like is indeed happening today, beginning to happen today in the area around Science Park.

Notwithstanding this progress, Science Park's gains are fragile, and the basic economic and social forces which had engulfed our neighborhoods are only being held at bay. Every day, as a real estate project in a blighted environment, Science Park must compete in the arena of business firms making hard business judgments concerning where to locate their operations and how best to gain an economic advantage over their own competitors.

I believe, therefore, that only if the Enterprise Zone Program is made responsive to the basic competitive dynamics of small business decisionmaking will Enterprise Zones bring the economic change and community benefit of the small business sector to the inner city. Inasmuch as national experience has shown that both technological innovation and new job creation flourish in small companies, I believe that Enterprise Zones can, if properly structured, create real economic progress where it is needed most.

To accomplish this goal, I would submit that Enterprise Zone benefits should be broadly conceived—and I am pleased that S. 58 certainly takes that approach—and should create direct benefit to businesses by operating through the Internal Revenue Code, for example. Enterprise Zone benefits can be made particularly responsive to the needs of small business if they focus on expediting and simplifying Federal Government process or providing technical assistance to growing small businesses.

Enterprise Zone benefits should be structured to induce private financing for companies doing business within zones, and therefore should be responsive to the financing entities as well. The Enterprise Zone mechanism should create strong inducements to support the innovation process itself for the purposes of promoting economic diversification; and I am thinking there of promoting research activities through the Small Business Innovation Research Program, for example, or with respect to direct Federal research expenditures. The Enterprise Zone Program should be used to promote investment by small businesses in fixed assets that will encourage their long-term commitment to a single location.

This is a short list, but it is intended to illustrate ways in which Enterprise Zones can alter the direct relationship between the Federal Government and individual companies so as to benefit inner city economic development. To be effective, I think Enterprise Zones must also address the physical environment of the inner city. Benefits designed to induce development of or investment in Enterprise Zone real estate could be an enormous inducement to economic growth in the city. And in a complementary fashion, giving priority for Federal infrastructure and transportation expenditures—and I believe Congresswoman Oakar made reference to this as well—in Enterprise Zones would directly address the physical decay and isolation which is so often characteristic of sites in areas which have lost their economic viability over time.

An Enterprise Zone Program which seeks to address the full range of challenges in the inner city must also grapple with the issue of creating community benefit, as well as economic development. It is simply not, I would submit, adequate to assume that economic renewal automatically will bring community renewal. Enterprise Zones should therefore benefit from priority funding under Federal employment and training programs, and programs which support the building of local community institutions should be targeted for Enterprise Zone benefits as well. And I am thinking specifically there of the Federal Community Development Block Grant, for example, which I know has been used in New Haven to support nonprofit, community-based development organizations.

The Enterprise Zone concept could be very effectively applied to address other critical urban issues as well, which are directly related to economic development projects like Science Park, such as housing. A critical housing initiative adjacent to Science Park, which is a terribly important complement to our economic development activities, would be greatly assisted, for example, if the benefits available under the Enterprise Zone Program include inducements to investment in housing development or benefits to those purchasing housing within Enterprise Zones.

Allow me to summarize, if I may. Rebuilding the inner city can only be accomplished through a comprehensive strategy. An effective Enterprise Zone Program must provide this kind of comprehensive strategy. It must provide inducements directly to business institutions to locate in an inner city location and to perform the kind of work there that will build a new, competitive economy for the future.

It must support other initiatives, such as employment, community development, housing, or law enforcement. And I have not mentioned law enforcement before, but this is critical to the stability of life in the inner city. These kinds of other initiatives, which will also ensure that the people of inner city America benefit from this kind of economic renewal.

There is one final point which I believe needs emphasis today as well. To maximize the effectiveness of the Enterprise Zone initiative, it is imperative, I think, that selection of zones be based not only on criteria which look to social and demographic factors, but also to criteria which will enable the Department of Housing and Urban Development to analyze the effectiveness of existing measures underway in the proposed zone to deal with the problems that exist there. And this was a comment that Commissioner Heintz made earlier.

Enterprise Zones are fundamentally an attempt to induce private investment in business activity and real estate development, and therefore, I think they can only be really effective in achieving that objective to the extent that other measures are simultaneously underway which will have the effect of promoting that kind of private sector investment. The current method in the existing legislation of definition and designation of Enterprise Zones has created problems and anomalies for the city of New Haven, I know, in attempting to meet HUD's requirements. And I have brought with me, Senator Lieberman, a letter from Ed DeLieto to yourself which specifies some of those issues and the kinds of problems which we have had in putting together the city of New Haven's zone application.

Beyond these technical issues, I think, lies something even more fundamental, which is that only by putting the Enterprise Zone resources into areas which not only have the problems which the program is designed to remedy, but also have the projects and partnerships underway to remedy those problems, will Congress achieve maximum effect through the Enterprise Zone Program for the dollars it spends.

Thank you again.

[The prepared statement of Mr. Ginsberg follows:]

TESTIMONY OF WILLIAM W. GINSBERG
PRESIDENT, SCIENCE PARK DEVELOPMENT CORPORATION
BEFORE THE UNITED STATES SENATE, COMMITTEE ON SMALL BUSINESS
CONCERNING ENTERPRISE ZONES AND SMALL BUSINESS
WASHINGTON, D.C.
JUNE 21, 1989

Senator Lieberman, Senator Boschwitz, Ladies and Gentlemen:

I am deeply appreciative of the opportunity to appear before you this morning and to address what I consider to be an issue of great importance to urban development policy in this country. I appear before you in my capacity as President of Science Park Development Corporation, a not-for-profit corporation which is developing an eighty-acre formerly abandoned industrial site in the inner city Dixwell/Newhallville neighborhood in New Haven, Connecticut into a high technology business and research park. I also bring to this hearing the perspective of one who has recently completed four years in city government in New Haven, as Mayor DiLieto's senior economic development staff person.

The challenge of economically abandoned inner city neighborhoods is, for Science Park and cities like New Haven, both the challenge of physical redevelopment and the challenge of business development. These are two very different challenges. I particularly welcome the opportunity to address myself to the topic of enterprise zones, because I believe that the enterprise zone program properly conceived represents an opportunity to marry these two very different and very important elements of the urban development challenge. The enterprise zone can be a potent tool to help comprehensively address the issues of urban America, by building a new economy for economically ravaged communities in our cities, and by seeing to it that that economic benefits which result are located and remain in those very communities.

This dual role is precisely what we are trying to accomplish at Science Park. Science Park is creating a new economy through technology business development; we have created one of the largest technology business incubators in the United States from the ashes of the eighty-acre former Olin Corporation industrial site in the heart of inner city New Haven. Science Park grew out of the commitment of the Olin Corporation to donate our eighty-acre tract over time for a technology business park. Our industrial facilities on Winchester Avenue in New Haven epitomize the difficulty which manufacturers in cities like New Haven have faced and continue to face in competing with domestic and with foreign

alternatives. This inability to compete led to an economic decline in the heart of New Haven of such severity that the working population at our facilities fell from a peak of over 20,000 during World War II to under 1,000 by the time Science Park was created in 1981. The Science Park strategy has been to create fundamental change in that cycle of economic decline, to create a new competitive economy through promoting innovation and to promote innovation through the application of technology. The strategy of Science Park has been based on the view that technology could and should flourish at our location, which is immediately adjacent to one of the great research universities of the world, Yale University. Yale has been a partner and a supporter of Science Park since its inception. This strategy of creating fundamental economic change through a new innovation-based economy has been implemented through incubating technology businesses.

Science Park has been amply and generously supported in this effort by the State of Connecticut and the City of New Haven. We have particularly benefitted by the designation of Science Park and the surrounding area as an Enterprise Zone under the State of Connecticut program.

Science Park has thus spent seven years toiling in this vineyard of economic change and community renewal. Our story demonstrates that through creation of a new economic base of applied technology, jobs can be created, private business institutions attracted, community institutions strengthened, and economic change made to work directly for the benefit of inner city neighborhoods which have suffered through two generations of steady economic decline. Today, Science Park is one of the largest and most successful small business incubators for technology companies in the United States: we house approximately 100 firms engaged in the production of goods and delivery of services which are technology related. Science Park has reversed the fundamental cycle of economic decline: in an area characterized by two generations of disinvestment, over $46 million has been invested in Science Park since 1982, and in an area characterized by two generations of steady job loss, Science Park has created or retained well in excess of 1,000 jobs during that time period. Science Park's most successful company, which began as the brainchild of two entrepreneurs operating out of a single office in 1983, is today a firm employing approximately 120 persons and operating as a division of Eastman Kodak, which purchased this company in 1987. Indeed, the Science Park strategy of carefully nurturing start-up technology companies is the one strategy which has succeeded in recent years in luring a major investment by a Fortune 500 company to the city of New Haven.

The community renewal which we have looked to as an indispensable companion to economic development is also occurring. In addition to the jobs created, over 1,000 persons have received various forms of job training in Science Park in recent years. Science Park has also created important partnerships with local community-based organizations to promote housing and commercial development in the surrounding areas. Housing and other important neighborhood development is happening around Science Park today. The economic benefits of the Science Park investment is being felt locally.

Science Park as a project has thus had its share of successes, and has even begun to reverse the fundamental cycle of economic decline that has plagued our site and our communities for many years. But these gains are fragile, and the basic economic and social forces which have engulfed our communities are only being held at bay. Every day, as a real estate project in a blighted environment surrounded by decay, despair and disinvestment, Science Park must compete in the arena of business firms making hard business judgments concerning where their operations should be located and how best to gain an economic advantage over their own competitors. In that arena, Science Park must compete both in terms of the environment which it offers companies and in terms of the bottom line cost of doing business in that environment. Let me then state an important part of my thesis: if the enterprise zone program can be made responsive to the basic dynamics of small business decision-making and the basic competitive issues which small business faces, then I believe that enterprise zones can bring the economic change and community benefit of the small business sector to the inner city. Inasmuch as national experience has shown that both technological innovation and new job creation flourish in small companies, I believe that enterprise zones can create real economic progress where it is needed most.

Allow me to make several general comments as to the kinds of programmatic benefits which, if offered in enterprise zones, would be directly responsive to the needs of small innovative technology businesses. These benefits should be broadly conceived, and should create direct benefit to businesses, by operating through the Internal Revenue Code, for example. Enterprise zone benefits can be made particularly responsive to the needs of small business if they focus on expediting and simplifying federal government process, or providing technical assistance to nascent small businesses.

Enterprise zone benefits must be structured to induce both outside investment in and outside loans to companies doing business within zones. The enterprise zone mechanism should

create strong inducements to support the innovation process itself, such as using the Internal Revenue Code to promote research activities in enterprise zones or providing priorities for enterprise zone companies under the Small Business Innovation Research program or with respect to direct federal research contracts. The enterprise zone program should be used to promote investment by small businesses in fixed assets that will encourage their long-term commitment to a single location. This is but a short list, but is representative of some of the many ideas which I know are being discussed in the Congress today to promote the kind of activities we are discussing. Fundamentally, this list is illustrative; it is illustrative of ways in which enterprise zones can alter the direct relationship between the federal government and these individual companies so as to benefit inner city economic development.

The competitive challenge faced by Science Park requires also addressing the environment at Science Park. Benefits designed to induce development of and investment in enterprise zone real estate could be an enormous inducement to economic growth in the inner city. In a complementary fashion, giving priority for federal infrastructure and transportation expenditures to enterprise zones and projects benefitting enterprise zones would address directly the physical decay and isolation so often characteristic of sites which have lost their economic utility.

Science Park seeks not only to create a competitive new economy for inner city New Haven and to rebuild an eighty-acre site, but also to make that new economy and that physical development directly benefit the Dixwell and Newhallville neighborhoods in New Haven. An enterprise zone program which seeks to address the full range of challenges in the inner city must grapple with this issue as well; it is simply not adequate to assume that economic renewal automatically will bring community renewal. By virtue of being defined geographically, enterprise zones are an excellent vehicle to promote this kind of comprehensive urban development strategy. Enterprise zones should therefore benefit from priority funding under federal employment and training programs. Programs which support the building of local community institutions should be targeted to enterprise zones as well. I am thinking specifically here of programs like the Community Development Block Grant, which have been used in New Haven to support non-profit community-based development organizations.

I would note too that the enterprise zone concept could be very effectively applied to address other critical issues which are a part of the urban development challenge. I am

thinking of housing as an example. Science Park's immediate neighbor to our south, sitting directly between the Science Park site and the Yale University campus, is a now-abandoned 366-unit high-rise public housing project called Elm Haven, which has been approved for demolition by the Department of Housing and Urban Development. Elm Haven is to be replaced by 400 new housing units. The opportunity exists to reintroduce a private housing development dynamic to the area, and to create new connections between the Yale University community, the Science Park community and what has been heretofore a largely isolated low income minority community in the Dixwell neighborhood. This entire area is along with Science Park part of the currently pending City of New Haven enterprise zone application. This housing initiative, which is such an important complement to Science Park's strategy of economic change, would be greatly assisted if the benefits available under the enterprise zone program included inducements to debt and equity investments in housing development, as well as benefits to those purchasing housing in enterprise zones.

The thrust of my argument can perhaps be summarized this way: urban development in the sense of rebuilding the inner city can best be accomplished - can indeed only be accomplished - through a comprehensive strategy. An effective strategy must address the physical rebuilding of the infrastructure and facilities of the inner city. But a comprehensive strategy must do much more than that. It must provide inducements directly to business institutions to locate in an inner city location and to perform the kind of work there that will build the new competitive economy of the future. And it must support other initiatives which will insure that the people of inner city America benefit from this kind of economic renewal such as employment, community development, housing or law enforcement, the latter of which I have not mentioned but which is so important to the stability of life in the inner city. It is this kind of comprehensive approach that we are attempting to implement at Science Park. It is, I believe, this type of comprehensive approach that should underlie Congress's approach to the creation of enterprise zones in the inner city.

There is one final point which I believe needs strong emphasis today. The enterprise zone concept can be a critically important piece of an overall urban development policy, if it embraces the multi-faceted challenge which we are confronted with today in the inner city. To maximize the effectiveness of the enterprise zone intiative, it is imperative that selection of zones be based not only on criteria which look to social and demographic factors, but also to criteria which will enable the Department of Housing and

Urban Development to analyze the effectiveness of other measures underway in the proposed zone to deal with the problems that exist there. Enterprise zones are fundamentally an attempt to induce private investment in business activity and real estate development. Enterprise zones can only be effective in achieving that objective to the extent that other measure are simultaneously underway which will have the effect of promoting that kind of private sector investment. The current method of definition and designation of enterprise zones has created problems and anomalies for the City of New Haven in attempting to meet HUD's requirements; I have attached a letter from Mayor DiLieto indicating the kinds of problems to which I refer. Beyond these issues lies something even more fundamental: that only by putting their enterprise zone resources into areas which have not only the social and economic problems which need to be remedied but also the projects and partnerships underway to remedy those problems will Congress achieve maximum effect through the enterprise zone program.

Thank you.

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BIAGIO DILIETO
MAYOR

OFFICE OF THE MAYOR

CITY OF NEW HAVEN
CONNECTICUT 06510

June 19, 1989

Senator Joseph Lieberman
United States Senate
Committee on Small Business
Washington, D.C. 20510

Dear Senator Lieberman:

During your review of the Federal Enterprise Zones legislation I would like to urge the Committee and HUD to revise the designation process from one based strictly on "distress" criteria to one that places more importance on the applicant city's and state's commitments to improving business and living conditions.

While I can appreciate the reasoning for using census based "poverty or distress" indicators, the final Federal Enterprise Zone boundaries that we submitted to HUD excluded some of the most distressed areas we had hoped to include. This was due to the strict reliance on 1970-1980 census data without regard to current conditions, and the inability for the zone to overlap into certain census tracts that are above poverty level minimums yet contain very distressed blocks.

In addition, certain projects already underway in our existing Enterprise Zone could not be included due to the sole reliance on census data.

The result is that the proposed Federal Enterprise Zone covers less than half of our existing State Enterprise Zone (see attached map).

In excluding over half of our existing Enterprise Zone the HUD eligibilty criteria eliminated two major projects which are essential to the ultimate success of the zone. Ironically, the Federal government, through HUD and the EDA, has provided approvals and funding for certain project activities.

In one case an entire block of public housing abandoned in 1984 could not be included in the Federal Enterprise Zone because the application required we use 1970-1980 census data. (See A on attached map.)

In the other case, our showcase project in the Enterprise Zone, the Science Park, had to be divided in half because a large portion lay in a census tract that itself is divided economically and therefore does not meet the 20% minimum poverty level.

A considerable degree of thought and analysis was put into developing our exicting State Enterprise Zone and its programs. I feel strongly that the Federal process for designating Federal Zones should take these factors into consideration.

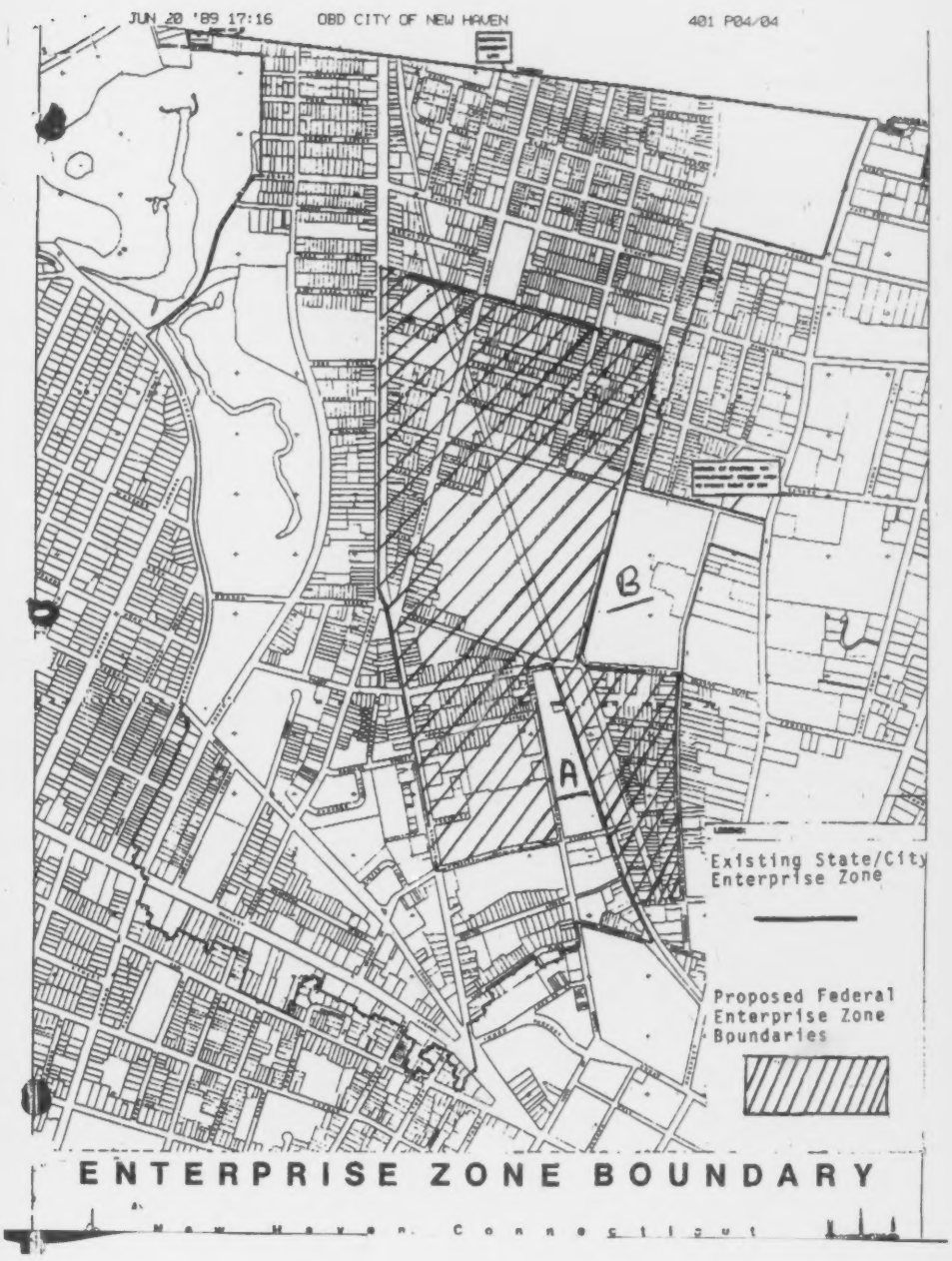
Thank you for your consideration on this matter and if I or my staff could provide further testimony or assistance please contact me.

Yours truly,

Biagio DiLieto

Mayor Biagio Dellieto

Encl.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Existing State/City Enterprise Zone
Proposed Federal Enterprise Zone Boundaries
ENTERPRISE ZONE BOUNDARY
New Haven, Connecticut

Senator LIEBERMAN. Thank you again. The three of you were outstanding and very helpful. You are all out there trying to make this program work, and I sense from each of you that you have achieved some success, but clearly there is a way to go.

I would guess that you have had a chance to look over S. 58 in general, and I would ask you this, dealing with the businesses that you are dealing with, trying to get them to come into the Enterprise Zones, what are the two or three most important incentives that we at the Federal level could give you to help you make the zones work?

Mr. GINSBERG. I deal specifically and our market specifically is in the technology sector which is related, I think, to the notion of diversification of an economy that is ultimately in recent decades has failed the communities where it is located.

And I think in that particular case, I would emphasize the point which I made in my prepared remarks relative to supporting research and development activities, an example being the SBIR Program, which exists in many Federal agencies which has been very important to starting small technology companies in Science Park, not only to getting contract funding to get these companies up and under way, but also to develop the new technologies which in turn provide a very good business base for those companies to prosper.

That is an example of the kind of research-oriented activities that I think are very important.

Senator LIEBERMAN. So, R&D credit is important?

Mr. GINSBERG. I think it is and more generally anything that goes to the financing for these companies—and I made reference to this also.

I think it is very important.

Senator LIEBERMAN. Initial financing?

Mr. GINSBERG. Indeed.

Senator LIEBERMAN. There are some pretty strong incentives in this bill for encouraging many to flow into new businesses in Enterprise Zones, deductibility of initial investments, being able to write off losses.

Mr. GINSBERG. That is terribly important.

Ms. DAWES. For us it is extremely important that there are strong incentives that are going to encourage the employers to hire from the area.

Currently the situation is that a number of employers decide to move into the zone based on the availability of a labor pool that they cannot find, at times, in suburbia.

However, once in the zone when they attempt to hire and retain, there is a tremendous problem with turnover. We all recognize that, in many instances, in an inner city neighborhood, residents lack skills and we also know that the work ethic, for various reasons, is not necessarily there. So that any incentive that is going to lessen the expense of the employer as he or she assumes the responsibility and the benefit, of course, of hiring from the community is going to be a tremendous plus.

Additionally, financing is an important incentive. We have many smaller businesses that have moved into the Enterprise Zone or are interested in moving into the Enterprise Zone and it is very important that they have easy access to financing.

One thing that I did not elaborate on in testimony is that there is a whole other side to development of distressed zone communities. There is a whole aspect of physical improvement to the area, the investment that is made in the area when somebody comes in and renovates a particular type of building that is going to be available for other businesses.

If the developer comes in and makes tremendous renovations to real estate, it is a face-lift to the community, even if only two jobs—and this is my opinion—but even if it becomes a warehouse and only two jobs are created as a result. The renovation or physical improvement will spark additional interest in the community and larger employers will move in and the result will be job creation.

So, there are many facets to this picture.

Senator LIEBERMAN. I think that is a good point, and it goes to the earlier part of what you said which is that obviously the optimum here is to not only locate businesses in the Enterprise Zones but to make sure that they are employing people who live in that vicinity, that the location of the businesses themselves is a plus because otherwise, presumably, there would be either open land or empty buildings, and that is a beginning. We hope to build around it, but that is a plus.

But let me ask you this, and I think you were right on target. Is there a job training component now, for instance, to the Hartford Enterprise Zone? Is there anything you can do to bring services to bear to prepare employees from the neighborhood to work successfully for the businesses that are located there?

Ms. DAWES. There are some local programs through the pilot program that I mentioned, one of the subcommittees is involved in employment and training as well, and we have a variety of city and state agencies that are looking at how to target and how to develop some new programs that would help along that line.

However, there is still a need to go beyond that because when an employer hires someone, he knows that he or she is going to have to spend the next six months getting that person up to that entry level point. That employer is losing money, so job training is very important.

Senator LIEBERMAN. And you say again, just for me to crystallize it, that one of the most important aspects of a bill like S. 58 would be to create incentives for the employers to train and stick with employees who reside within that poor area?

Ms. DAWES. That is right. And to add a little bit more to what you are saying, we are looking for jobs with advancement potential. We are not looking to place residents in jobs that are dead-end.

Senator LIEBERMAN. Mr. Nathanson.

Mr. NATHANSON. Senator Lieberman, there is some fine-tuning that can be done to S. 58. I want to just echo what the other witnesses have said about the employment of target area residents in these businesses, and I think that that job training link to the businesses is very important.

For example, there is a provision in S. 58 now that says that an employee has to be employed for 270 days before the employer is able to take advantage of the disadvantaged worker job credit.

What we have proposed is that the time that a worker spends in a Job Training Program, particularly if it is a program where the employer is committed to hire that person when he completes a job training, that that time spend in the employment would count towards the 270 days. It is a small refinement, but it is a way that the legislation can be fine-tuned to create that employment link.

Senator LIEBERMAN. That is a helpful suggestion.

Senator BOSCHWITZ. I think that that is a good idea.

We are presently debating on the floor of the Senate the child care provision, and I want to relate it to some of your comments, particularly Mr. Ginsberg's comments.

There are two varying approaches on child care. I look at it in a very practical way. First, 81 to 84 percent of the child care providers in this country are not licensed. Second, most child care starts with a rather simple and basic premise and that is that a mother wants to stay home with her children, but has to provide some income for the family. She stays home with her children, thereby saving the cost of child care for her own child or children and takes in a few of the neighbors'.

In Minnesota we license. We have the largest licensing program in the country. The State of California has a population roughly six or seven times as large as ours and we license more child care providers, mainly because we do it in a reasonable manner. Child care providers have not been overwhelmed by the process of licensing; interestingly, the child care providers, the organization and the State are very supportive of a bill I introduced which is pretty much the Republican alternative, and that is to avoid new regulatory efforts initiated on the Federal level and to adopt tax credits instead, where the monies can go directly to the parents or the providers involved.

I think that in the event we try to regulate child care providers, they will all go underground. They will not want to report income for taxes or for whatever reason. I relayed all that because I respectfully say to you that we may be presuming more of this legislation than we are going to be able to deliver.

Mr. Ginsberg wants a comprehensive strategy and wants to integrate numerous Federal programs, and I think that is logical. Training programs, housing programs all should be integrated.

If we start up that way, very frankly, this legislation is going to go nowhere at all, and we are having trouble pushing it forward as it is. We have to try to keep it as simple as possible to get the legislation passed, then we will try to integrate it.

They say there is no regulation now, but wait until next year. There will be additional regulations, there will be additional steps that child care providers who have five or six children in their homes and have a gross income of $12,000 to $15,000 a year will have to go through. Those providers will simply abandon the system and go underground, as I express it.

So, do not expect more from this legislation than we can deliver. It is very hard, I think, for the Federal Government to set up legislation that is going to be able to distinguish among employers and what kind of jobs they provide and exactly whether or not they attract people who are the most dependent on perhaps some of the other programs of Government, and so forth.

It is important that we get it off the ground. I do agree that we ought to broaden the criteria of choosing the zone that you have mentioned, and I think that Mr. Nathanson's final suggestion is a good one. We ought to include in the period the efforts of training.

But do not expect more of us than we are going to be able to deliver because if you expect too much, we will not be able to deliver anything, I am afraid. We have had some problems in delivering to date. I just told a young friend of mine here that legislation is slow—and I was not used to that before I got here.

You said approximately 100 firms have moved into the Science Park, and it was not clear—you have created or retained well in excess of 1,000 jobs. You had 1,000 jobs there to start with, down from 20,000 or 25,000 during the Second World War. I forget the number, but how many have you created?

Mr. GINSBERG. Those numbers, approximately, Senator—you have to understand the history of it. This was the Winchester Olin facilities, as I think I mentioned.

Senator BOSCHWITZ. One of these old, big buildings?

Mr. GINSBERG. A big campus of buildings, 80 acres in fact, and 1,000 jobs created over time does not include the existing Winchester facility which remains, albeit in much shrunken form, as our next-door neighbor today.

So, the 1,000 jobs that are referred to as remaining in the park in 1981, that was basically the Winchester factory, and that employs about 700 people today. The 1,000 jobs created or retained are really over and above that. It involves a couple of divisions of Olin, which did not leave, and the rest of that, approximately three-quarters of that, 750–800 jobs, is new job creation from the firms which did not exist before or did not exist at Science Park before.

Senator BOSCHWITZ. You mentioned Eastman Kodak. How many firms have you been able to attract to this area?

Mr. GINSBERG. Most of the firms at Science Park are start-up firms, are firms that began at Science Park, and that has been what we have geared our efforts to.

The Eastman Kodak connection actually began as a start-up firm. It is the most successful firm in the park. It began as two entrepreneurs in 1983 with an idea and one office rented from us and today it is a division of Eastman Kodak.

Kodak purchased this company in 1987. They employ about 120 people, and Kodak paid $16 million for the company which was a success obviously, not only for those entrepreneurs who did very well by that, but also for the city. It is the only example in recent years of a Fortune 500 company making a major investment in New Haven, so it has got positive implications for the entire economy, I think.

Senator BOSCHWITZ. And a bunch of small companies that have come in?

Mr. GINSBERG. Yes.

Senator BOSCHWITZ. What kind of science-orientations have these companies had?

Mr. GINSBERG. Primarily computer science, biotechnology, Yale, and the Yale Medical Center, and the hospitals in New Haven are a real draw for the biotechnology field, but in terms of numbers it

is computer science more than any other in terms of numbers of jobs. It is biotechnology.

Senator BOSCHWITZ. I noticed as you went along here that you want all the programs of the Federal Government to focus in on these Enterprise Zones, and I wrote give us a break.

Mr. GINSBERG. If I could comment on that, Senator, the temptation to lay out a wish list, one does not get to give testimony before the U.S. Senate Committee on Small Business very often. The temptation to lay out a wish list was irresistible, and I certainly appreciate the strategic approach which is get the legislation adopted and then——

Senator BOSCHWITZ. I appreciate that.

Senator LIEBERMAN. Existing in New Haven, one is very practical, let me assure you.

Senator BOSCHWITZ. I presume so. As Ms. Dawes spoke, she appeared to be a very practical person trying to inter-relate some of the things that were being done on the State and local level.

You spoke about existing businesses in these zones. Do the existing businesses in your zones or in yours, Mr. Nathanson, get the same advantages? I guess the other gentleman from Minnesota answered that already, that an existing business in Minnesota's zone does not necessarily get the advantage—that all businesses do not have the same advantages within the zone.

Mr. NATHANSON. Senator Boschwitz, the way the process works in Minneapolis is that a firm located in the city of Minneapolis but outside of the zone can get the credit for moving into the zone. The choice facing many expanding businesses is to stay in the city or move out to the suburbs.

So, it is not merely moving from across the street into the zone to get the credit. The choice is moving to Franklin Avenue, and going out to Eden Prairie.

So, any business that is located in Minneapolis currently can receive the credit if they locate in a zone. Most often, we use the credits to encourage existing businesses to expand within the Enterprise Zone.

Senator BOSCHWITZ. We will have to address and we will have to talk about whether or not we can adopt the selectivity which you spoke about. It is not clear to me that we are going to be able to legislate that, and I do not want to do things that precede our own experience.

If we try to legislate too many bells and whistles, so to speak, we may end up not legislating at all. I want to be careful about that. But I enjoyed your testimony as well.

You know, I made a note that somebody mentioned bonus points for innovative ideas. I think we might have a hard time with that in putting together a bill. Have any of you looked at the earned income tax credit as a supplemental federal effort for your Enterprise Zones?

Mr. NATHANSON. Mr. Chairman, in an earlier job I was involved in welfare and income assistance programs so I am familiar with the earned income credit. I would say that it is an excellent tool, and I would hope that Congress might build on that concept. The credit is particularly significant because it is refundable for low income individuals. Somebody who is employed and does not have

much tax liability can get the benefits of the credit, and I think that that concept could be applied in this legislation.

Senator BOSCHWITZ. I like the earned income tax credit. I think it is well targeted, particularly towards families. My staff reminded me that I did not allow you, Ms. Dawes, to answer the question that I asked about transferring into the area from outside of the zone, whether or not they get all the same benefits. Do they in Connecticut?

Ms. DAWES. Existing businesses are very important. Could you repeat the question.

Senator BOSCHWITZ. Do all businesses existing and those who move into the zone get the same benefits in Connecticut?

Ms. DAWES. As long as there is a degree of expansion.

Senator BOSCHWITZ. When you find a business in the zone that does not expand, does it get any benefits?

Ms. DAWES. This has been quite interesting because when I started as an Enterprise Zone manager and introduced myself to the existing businesses, many were quite perplexed, and there was no benefit to them.

As a result, we have spent a great deal of time talking to existing zone businesses to discuss their needs. That is how we have determined needs such as procurement assistance and additional financing, sometimes just to stay in business.

In addressing needs, we try to put them in the context of what is important to an Enterprise Zone so that when we assist a business to obtain contracts, we provide the assistance in the context of possible future employment for residents in the area.

Senator BOSCHWITZ. Well, I thank the witnesses, Mr. Chairman, and I would say again that it is regretful that Secretary Kemp is not here, but I would not take that as being anything other than what it is, and that is that he is fighting the good fight within the Administration and trying to get some of them to understand.

Some of my friends in the Administration are not always so cooperative. The Reagan administration was not cooperative about this, even though it is a program that I would have thought would be more appealing to them. Unfortunately, it was not.

Now, as we go to a new Administration, we have some of the same problems. So, Jack is in there battling away, and knowing Jack, he is persistent and I think that we will eventually see legislation coming out of all of our efforts. I thank you, Mr. Chairman.

Senator LIEBERMAN. Thank you, Senator Boschwitz. It is really an honor to join you in this battle talking about battles, and I echo what you said about Secretary Kemp. I spoke to him this morning, and to say the obvious, he remains enthusiastic and undeterred. He is going forward.

I think he has found supporters, and if he identifies his opponents, he is going to try hard to convince them that he is on the right course.

The testimony has been very helpful. In my thinking this is not only critically important to areas that are poor in our Nation, both urban and rural, but it also is a test or it is an another application of a basic policy which I believe this Administration believes and I do myself which is that money moves to the point where it receives

more return, and money is logical in that sense, and that is true of capital in the most profound sense.

And what we are going to do here is to intervene in the marketplace to create some magnets, some incentives to move money to areas where it can not only create jobs and entrepreneurship, but can particularly benefit people in an area where that benefit is needed.

And, again, the more I get into it, senator Boschwitz has been fighting this fight for a while, and I am new to the Senate, obviously, and new to this battle. But, in my opinion, it is a very strong idea, and the testimony that has been offered today by the State and local witnesses has really deepened my own support for the idea because you are applying it, and I am particularly pleased that you think the incentives that are part of S. 58 which Senator Boschwitz has authored and I am pleased to co-sponsor really would be of help to you in doing what you want to do for your community.

I thank you very much for taking the time. I thank you particularly for the quality of your testimony which I think has been first rate.

The hearing is now concluded.

[Whereupon, at 12 noon the Committee recessed, subject to the call of the Chair.]

ENTERPRISE ZONE PROGRAM AND ITS IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT

THURSDAY, SEPTEMBER 21, 1989

U.S. SENATE,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met at 1:21 p.m., in room 428–A, Russell Senate Office Building, Hon. Joseph I. Lieberman and Hon. Rudy Boschwitz (Acting Chairmen) presiding.

STATEMENT OF HON. RUDY BOSCHWITZ, A U.S. SENATOR FROM THE STATE OF MINNESOTA

Senator BOSCHWITZ. Mr. Secretary, if you will sit down, perhaps we can begin with opening statements. We will start with opening statements and wait for Senator Lieberman. In consideration of your time limitations Mr. Secretary, I recommended that we begin.

We are very pleased to have Secretary Kemp here today. He is really the originator of the whole idea of Enterprise Zones, and carried it so skillfully during his days in the House. I, along with Senator Kasten and others attempted to do the same here in the Senate.

There is no question that it is an idea whose time has come and, in fact, came some time ago. The need seems to become more and more accentuated. The idea of creating employment rather than creating additional welfare programs is so appealing. I just heard last night, as a matter of fact, from Senator Bond on the Senate floor. He talked about giving a person the ability to provide for himself, giving him a hook rather than the fish. I think he was responding to an amendment that was offered last night. And that's really what Enterprise Zones intend to do.

It is a pleasure to have you here, Mr. Secretary, and we look forward to your testimony.

[The prepared statement of Senator Boschwitz follows:]

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STATEMENT OF SENATOR RUDY BOSCHWITZ

FOR THE

SMALL BUSINESS COMMITTEE HEARING ON

ENTERPRISE ZONES

I WANT TO BEGIN BY WELCOMING OUR PANEL OF DISTINGUISHED WITNESSES WHO HAVE TAKEN TIME FROM THEIR SCHEDULES TO TESTIFY ON THE ISSUE OF ENTERPRISE ZONES AND THEIR IMPACT ON SMALL BUSINESS. THIS IS OUR SECOND HEARING ON THIS TOPIC, YET IT COMES AT AN IDEAL TIME. CONGRESS IS IN THE PROCESS OF CONSIDERING TAX AND APPROPRIATIONS BILLS.

THERE HAVE BEEN VARIOUS MEASURES PROPOSED TO ATTACK THIS NATION'S SOCIAL AND ECONOMIC ILLS. TRADITIONALLY, WE HAVE CHOSEN TO SPEND LARGE SUMS OF MONEY TO RESOLVE THE PROBLEM OF ECONOMIC BLIGHT THROUGH THE CREATION OF WELFARE INSTITUTIONS. TODAY, WELFARE OBLIGATIONS ABSORB NEARLY HALF THE FEDERAL BUDGET. ADMITTEDLY, SOME ANTI-POVERTY PROGRAMS PROVIDE CRUCIAL SERVICES TO THE MOST DISTRESSED IN OUR POPULATION. BUT, ON THEIR OWN, THEY DO NOT APPEAR TO ACHIEVE THE RESULTS WE NEED TO RAISE THE LIVING STANDARDS OF ALL AMERICANS.

SECRETARY KEMP SAID IT BEST IN HIS RECENT EDITORIAL IN THE **WASHINGTON POST**. THE GREAT SOCIETY PHILOSOPHY FALLS SHORT IN THE EFFORT TO HELP THE POOR HELP THEMSELVES. ENTERPRISE ZONE ADVOCATES RECOGNIZE THE BENEFITS OF ECONOMIC OPPORTUNITY, JOBS, AND ACCESS TO INCOME AS TOOLS TO MAKE FREEDOM A REALITY FOR THE SOCIALLY AND ECONOMICALLY DISADVANTAGED.

THE IMPACT OF JOBLESSNESS IS PAINFULLY EVIDENT. DRUG ABUSE AND CRIME ARE ON THE RISE. INSTITUTIONS SUCH AS FAMILIES, SCHOOLS

AND CHURCHES WHICH FORMERLY IMBUED OUR CHILDREN WITH PRODUCTIVE VALUES ARE CRUMBLING BEFORE OUR EYES. AND YET, AS SECRETARY KEMP POINTED OUT IN THE **POST**, "THE THRIVING URBAN UNDERGROUND ECONOMY - NOT JUST DRUG SALES BUT EVERYTHING FROM BARTERED PLUMBING AND HOUSE PAINTING TO INFORMAL DAY CARE - DEMONSTRATES THAT [DEPRESSED] AREAS ARE RICH IN ENTREPRENEURIAL POTENTIAL."

ENTERPRISE ZONES WOULD PROVIDE A WAY TO CHANNEL AND REWARD THAT POTENTIAL. THEY WOULD ENCOURAGE JOB CREATION THROUGH A FEDERAL/STATE/LOCAL PACKAGE OF TAX BENEFITS AND OTHER INCENTIVES OFFERED TO BUSINESSES THAT LOCATE OR EXPAND OPERATIONS IN A DESIRED ZONE.

IN THE SENATE, LEGISLATION ON ENTERPRISE ZONES HAS BEEN EVOLVING SINCE THE BEGINNING OF THE DECADE. MY URBAN JOBS AND ENTERPRISE ZONE ACT OF 1980 AND THE HOUSE COMPANION BILL, INTRODUCED BY THEN-CONGRESSMAN JACK KEMP, WERE THE SEED FROM WHICH THE ENTERPRISE ZONE IDEA GREW. THE FULL SENATE PASSED MY ENTERPRISE ZONE BILL IN 1983 AND IN 1984. UNFORTUNATELY, BOTH TIMES IT WAS DROPPED BY THE CONFERENCE COMMITTEE.

MORE RECENTLY, IN 1987, THE HOUSING AND COMMUNITY DEVELOPMENT ACT WAS ENACTED INTO LAW. TITLE VII OF THE ACT PROVIDES FOR THE ESTABLISHMENT OF 100 ENTERPRISE ZONES, ONE-THIRD OF THEM IN RURAL AREAS. WHILE THE ACT ALLOWS THE SECRETARY OF HUD TO WAIVE REGULATORY RESTRICTIONS AND LOCAL AND STATE GOVERNMENTS TO TRANSFER MONEY FROM OTHER SOURCES TO THESE ZONES, IT DOES NOT

PROVIDE ANY FEDERAL INCENTIVES TO COMPLEMENT LOCAL INITIATIVES. MY ENTERPRISE ZONE IMPROVEMENTS ACT OF 1989 CALLS FOR FEDERAL INCENTIVES IN THE FORM OF TAX CREDITS FOR EMPLOYERS AND EMPLOYEES IN BUSINESSES LOCATED WITHIN A DESIGNATED ENTERPRISE ZONE.

I WOULD LIKE TO CONCLUDE BY SAYING THAT I LOOK FORWARD TO TODAY'S TESTIMONY. YOUR COMMENTS WILL ASSIST US IN FORMULATING WORKABLE ENTERPRISE ZONE LEGISLATION.

Senator BOSCHWITZ. I now turn to my friend, Senator Kasten.

STATEMENT OF HON. ROBERT W. KASTEN, JR., A U.S. SENATOR FROM THE STATE OF WISCONSIN

Senator KASTEN. Rudy, thank you.

Let me also just make a brief statement, first of all, to welcome Jack. We are delighted to have you here with us today, and we are lucky to have with us, Rudy, one of the most important intellectual leaders in America. Over the past 2 decades Jack Kemp has promoted many bright and innovative new approaches to the challenges facing America.

One of the most important ideas promoted by Secretary Kemp in my opinion has been Enterprise Zones. At a time when the war on drugs is focusing our national attention on the crisis of our inner cities, we ought to be doing all we can to provide alternative futures for the young people of these communities. A writer for the New Republic recently commented that when all the choices you have before you are bad ones, using crack becomes a more and more attractive choice.

Enterprise Zone legislation would give inner city residents a broader spectrum of choices, by creating jobs, by boosting small business startups, for providing a way up and a way out. Enterprise Zones would decrease the fatal attraction which dangerous drugs hold for young men and women.

Last year when Secretary Kemp was still in Congress, he and I co-sponsored a comprehensive bill of pro-growth tax cuts which included an Enterprise Zone provision. And as recently as this week in the Washington Post, Secretary Kemp called on Congress to pass Enterprise Zones this year as part of our overall tax package.

Secretary Kemp recognizes that the solution to our drug crisis, our crime crisis and the crisis of inner city despair is to unleash the potential of the people themselves, and we can do this with a capital gains cut, Enterprise Zones and other pro-growth measures.

Jack, we thank you for being here today. Enterprise Zone legislation has been around for over 10 years, and frankly I think American inner cities have waited long enough. I look forward to your testimony today as we start to piece together a dynamic new Enterprise Zone package in the 101st Congress, one that we can pass, that we can enact into law and that I know the President of the United States will enthusiastically endorse.

Thank you, Mr. Chairman.

Senator BOSCHWITZ. Senator Bond.

STATEMENT OF HON. CHRISTOPHER S. BOND, A U.S. SENATOR FROM THE STATE OF MISSOURI

Senator BOND. Thank you, Mr. Chairman.

I sincerely believe that small business and Enterprise Zones are recipes for revitalization of many of our economically distressed areas. And I'm delighted that Senators Boschwitz and Lieberman have pushed for this hearing today, and I thank you both.

In addition, I am very pleased to have the opportunity once again to hear Secretary Kemp's eloquence on this program. He was

an inspiration to us in Missouri. He helped us as we implemented the program which he conceived and fought for so strongly.

Mr. Chairman, I have long been a supporter of Enterprise Zones because I believe they are an extraordinarily useful tool in dealing with the problems of unemployment and under-employment in our small towns and in our urban areas.

For example, Missouri's rural economy has been profoundly affected by the changes in agricultural practices. The move toward capital-intensive and away from labor-intensive farming operations resulted in noticeable declines in the number of jobs available in rural America. In fact, in many out-state counties of Missouri, the biggest source of income has become the transfer payment—Social Security and other retirement benefits for elderly citizens. This means that young people are forced to leave the small towns to find jobs.

As we looked at these problems in Missouri back when I was Governor in the early 1980s, one of the solutions which I recommended and was eventually able to sign into law was the idea of an Enterprise Zone. We developed bipartisan support for it. We signed it into law and we put it into action. It went into effect in 1983.

It requires the area to meet relevant economic need and unemployment criteria in order to receive an Enterprise Zone designation. Once designated, a business can claim an investment tax credit against its State taxes for 10 years. A company can also take $1,200 in tax credits for each job it creates for unemployed individuals who live in the Enterprise Zone and $400 per person if it has to provide specialized training. Finally, half of the new company's income is eligible for an exemption from state tax for up to 15 years.

Now, Mr. Chairman, there has been some question raised about whether these incentives work. In particular, a Washington Post story of February 19 of this year raised a series of concerns about the effectiveness of our St. Louis Enterprise Zones. I'll comment on that article later, but let me assure you that the Missouri program has been a tremendous success, and Secretary Kemp visited that program.

I will say in summary that, with our St. Louis Enterprise Zone, we got far more bang for the buck, more jobs created per dollar than any other Federal direct grant program that we used. In Missouri 33 Enterprise Zones have been designated. They resulted in over 8,000 new jobs and nearly $800 million in investment in new plant and equipment. We have had successes in Saint Joseph, Springfield, Salem, Perryville, as well as in our metropolitan areas.

In summary, Mr. Chairman, areas of our country have taken a real beating over the past several years. They are an important part of our economic and social fabric. They must not be abandoned. I sincerely believe that Enterprise Zones are a practical and valuable tool for helping revitalize these areas in need and certainly join you in hoping that Congress will move to pass legislation this year.

I look forward to hearing Secretary Kemp's remarks.

I would digress only 1 minute to say that many of us, and myself particularly, want to commend the Secretary because he has had to move forcefully to deal with administrative problems in the agency

he inherited. The fact that these problems have been in some instances almost overwhelming have not deterred him from coming forward with constructive new proposals, and continuing to work to develop programs that can help now and in the future, even as he works to clean up some of the problems of the past.

Thank you, Mr. Chairman. I look forward to the Secretary's remarks.

STATEMENT OF HON. JOSEPH I. LIEBERMAN, A U.S. SENATOR FROM THE STATE OF CONNECTICUT

Senator LIEBERMAN. Thank you. I'm sorry to be here late, but delighted to be here and particularly pleased, Secretary Kemp, to have you here and to join with my colleague from Minnesota, Senator Boschwitz, and other Members of this Committee for this second hearing on Enterprise Zone legislation.

In 1961 President Kennedy said that, "Economic growth has come to resemble the Washington weather. Everyone talks about it, no one says precisely what to do about it, and our only satisfaction is that it can't get any worse."

For too long that has been the general reaction to economic health or economic sickness, particularly in our urban areas. And I commend you, Secretary Kemp, and I am pleased to join with you, Senator Boschwitz, for not just talking about economic growth, but for trying to do something about it with this Enterprise Zone legislation.

The first Enterprise Zone legislation in this country was introduced by two Members of Congress, one is right before us, Congressman Kemp, Republican from Buffalo, and Representative Bob Garcia, Democrat from the South Bronx. And what brought these two men together was the desire to find a long-term solution to poverty while stimulating economic development across our Nation. Ultimately in 1987 Enterprise Zone legislation was passed into law as part of an omnibus housing bill.

In essence, that bill directed the Secretary of Housing and Urban Development to designate 100 Enterprise Zones across the country, but it did not provide for any corresponding Federal tax benefits, as you know. And that's precisely what the bill that Senator Boschwitz and I have introduced would do. It would put into place the tax and regulatory incentives which we believe are pivotal to the success of Enterprise Zones and the redevelopment of urban and rural America.

Our bill attempts to bring benefits to impoverished areas without incurring an overall loss of revenue. It is important, however, as I know you feel, Mr. Secretary, to look beyond the statistics and consider the social impact that the Enterprise Zone Program can have on a community by giving its residents jobs and a new sense of hope about their future. The Enterprise Zone Program in its very essence assumes that investment in employment directed to geographic areas that have had a history of low levels of economic activity provide benefits to society in excess of what would be obtained if the investment in employment were directed to areas that already have experienced healthy economic growth.

Now, I believe and I would guess all of us here believe that the Federal Government cannot act alone in tackling these problems. We must work with business and industry in developing what might be called a holistic strategy that will attack chronic poverty, and the Enterprise Zone concept is clearly a way to do that.

Currently 37 States have begun this process with Enterprise Zones. I am pleased to say that Connecticut actually led the Nation in 1982 with the first proposal. In June our own Commissioner of Economic Development testified before this Committee that over the past 6 years, Connecticut's zones have created nearly $400 million of new investments and created or retained more than 13,000 jobs.

Winston Churchill—I take pleasure in saying this, and I believe you are a fellow Churchillophile, Mr. Secretary. Is that true?

Secretary KEMP. We are.

Senator LIEBERMAN. We share that affliction, that devotion.

Secretary KEMP. DEVOTION.

Senator LIEBERMAN. You are familiar with the quote I'm sure when he said that, "Some see private enterprise as a predatory target to be shot, others as a cow to be milked, but few are those who see it as a sturdy horse pulling the wagon."

The most appealing feature of Enterprise Zones, I think, is their attempt to involve and utilize private enterprise in doing something substantial on a national scale about chronic poverty, poverty that not only encompasses whole sections of every one of our inner cities, but also in too many cases spans generations. That's a cloud over our Nation and its future, and I believe Enterprise Zones are one innovative way to remove the cloud.

I thank you for being here.

[The prepared statement of Senator Lieberman follows:]

For immediate release:
Thursday, September 21, 1989

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STATEMENT OF
SENATOR JOSEPH I. LIEBERMAN

SENATE SMALL BUSINESS COMMITTEE

ENTERPRISE ZONES AND THEIR EFFECT ON
SMALL BUSINESS GROWTH AND DEVELOPMENT

I am pleased to be here today with my friend and colleague from Minnesota, Senator Rudy Boschwitz for the second hearing on Enterprise Zone legislation before the Senate Small Business Committee.

The history of federal urban policy and declining urban economies is a relatively brief one dating only from the early 1960's. In 1961, John F. Kennedy said that "Economic Growth has come to resemble the Washington weather - everyone talks about it, no one says precisely what to do about it, and our only satisfaction is that it can't get any worse." Whether it was the Model Cities program in the 60's or revenue sharing in the 70's, urban development has been a challenge facing the Administration and the Congress for the last thirty years.

I commend Secretary Kemp and Senator Boschwitz for not just talking about economic growth, but for spending the better part of this decade advocating the concept of enterprise zones, an innovative approach to the re-development of some of our most distressed urban and rural communities.

An enterprise zone is a specific geographic area which is designated to receive special treatment by the local, state, and federal government in order to attract business investment, via a series of incentives, that might otherwise not occur. These incentives include a combination of tax relief, regulatory relief, and targeted financing to depressed regions.

Enterprise zones have been around for some time. Two Englishmen of diverse political philosophies, Peter Hall and Sir Geoffrey Howe first began working on this idea in the 1970's. It came to fruitation in 1980, when an enterprise zone program was enacted by Prime Minister Thatcher.

The first national enterprise zone legislation in this country was introduced by two Members of Congress also of diverse background, Representative Jack Kemp, a Republican from Buffalo, New York, and Representative Bob Garcia, a Democrat from the South Bronx, while Jimmy Carter was still President. What brought these two men together was a desire to find a long term solution to poverty while stimulating economic development across our nation.

Ultimately, in 1987, enterprise zone legislation was passed into law as part of an omnibus housing bill. In essence, this bill directed the Secretary of Housing and Urban Development to designate 100 enterprise zones across the country, but it did not provide for any corresponding federal tax benefits. That is precisely what the bill which Senator Boschwitz and I have introduced would do - put into place the tax and regulatory incentives which are pivotal to the success of enterprise zones and the redevelopment of urban and rural America.

Our bill attempts to bring benefits to impoverished areas without incurring an overall loss of revenue. It is important, however, to look beyond statistics and consider the positive social impact that the enterprise zone program can have on a community by giving its residents jobs and a new sense of hope about their future. The Enterprise Zone program in its very essence assumes that investment and employment directed to geographic areas that have had a history of low levels of economic activity provide benefits to society in excess of what would be obtained if the investment and employment were directed to areas that experienced healthy economic growth.

The federal government cannot act alone in tackling the problems of our inner cities and poorer rural areas. We must work with business and industry to develop a holistic strategy that will attack chronic poverty. Currently, 37 states have begun to do precisely this by establishing their local versions of enterprise zones. I am pleased to say that Connecticut led the nation in establishing zones in 1982, offering a wide range of state and local incentives, as well as administrative support, to help develop distressed urban areas.

At our June hearing, the Commissioner of the Connecticut Department of Economic Development, Steven Heintz, testified that over the past six years, Connecticut's zones have created nearly $400 million in new investment and the creation or retention of more than 13,000 jobs.

Winston Churchill said that "some see private enterprise as a predatory target to be shot, others as a cow to be milked, but few are those who see it as a sturdy horse pulling the wagon." The most appealing feature of enterprise zones is their attempt to involve and utilize private enterprise in doing something substantial on a national scale about chronic poverty. Poverty that not only encompasses whole sections of every one of our inner cities but also, in too many cases, spans generations. It is a cloud over our nation's future. The unemployed and the hopeless, whether they are in the Bronx, Bridgeport, East St. Louis, Watts, Minnesota, or Liberty City are a problem for us all. Enterprise zones offer one innovative solution to that problem.

Senator LIEBERMAN. I note the presence of Senator Kerry and Senator Dixon. The Senator from Massachusetts.

STATEMENT OF HON. JOHN F. KERRY, A U.S. SENATOR FROM THE STATE OF MASSACHUSETTS

Senator KERRY. Thank you, Mr. Chairman. I do not have an opening statement. I just want to welcome the Secretary. I appreciate his attention to a number of different issues in this area and have enjoyed the opportunity to visit some of them in Massachusetts, and I am very appreciative of his commitment and concern.

In addition to that, as I have said with him during our visit and at other times, he has been a longtime champion of the approach of Enterprise Zones. It has been too long in the coming. I am a strong supporter of it.

And I want to say that I have some suggestions which I will be offering in legislative form that I hope can add some other ideas and creative energy to this effort. Specifically I would like to go beyond simply a tax credit approach and see if we can perhaps create a revolving loan fund as part of the Enterprise Zone concept to address specific infrastructure demands and service demands within Enterprise Zone areas.

In addition, I am going to suggest that the high intensity drug zones so designated by Secretary Bennett be automatically designated Enterprise Zones, and I think there are a number of thoughts along these lines where we might be able to add to the concept.

Mr. Chairman, I am delighted to be here to be able to listen to this and to share in the effort. And I hope we can really move rapidly on this.

Senator LIEBERMAN. Thank you, Senator.

Senator Dixon.

Senator DIXON. Mr. Chairman, I have a statement I'll place in the record. I just want to say I'm delighted to see my good friend, Secretary Kemp here. We are looking forward to hearing from him.

[The prepared statement of Senator Dixon follows:]

SEPTEMBER 21, 1989

STATEMENT OF SENATOR ALAN DIXON

SMALL BUSINESS COMMITTEE HEARING
ON
ENTERPRISE ZONE PROGRAMS AND THEIR IMPACT
ON SMALL BUSINESS GROWTH AND DEVELOPMENT

MR. CHAIRMAN, I AM PLEASED TO BE HERE THIS AFTERNOON AS THE SENATE SMALL BUSINESS COMMITTEE CONTINUES ITS REVIEW OF ENTERPRISE ZONE PROGRAMS AND THEIR IMPACT ON SMALL BUSINESS GROWTH AND DEVELOPMENT. I WELCOME THE DISTINGUISHED GROUP OF WITNESSES BEFORE US. I KNOW THE COMMITTEE WILL FIND THEIR TESTIMONY ON THIS SECOND DAY OF HEARINGS TO BE INFORMATIVE AND HELPFUL.

I WANT TO TAKE THIS OPPORTUNITY TO WELCOME SECRETARY KEMP, WHO HAS BEEN A STRONG ADVOCATE OF ENTERPRISE ZONES THROUGHOUT THIS DECADE. I LOOK FORWARD TO HIS COMMENTS, AS WELL AS THE TESTIMONY OF OUR OTHER WITNESSES, WHICH WILL ASSIST THE EFFORTS OF THIS COMMITTEE IN FORMULATING EFFECTIVE ENTERPRISE ZONE LEGISLATION.

I AM A LONG-TIME SUPPORTER OF ENTERPRISE ZONES. I BELIEVE THAT SMALL BUSINESS PARTICIPATION IS THE KEY TO SUCCESS OF ANY ENTERPRISE ZONE PROGRAM, AS THEY ARE TO OUR NATION'S ECONOMIC WELL-BEING. SMALL BUSINESSES CONTINUE TO PROVIDE THE MAJORITY OF NEW JOBS AND TRAINING OPPORTUNITIES.

IT IS IN OUR BEST INTEREST TO ENCOURAGE SMALL AND LARGE BUSINESSES ALIKE TO LOCATE IN DEPRESSED AREAS, CREATING

MUCH-NEEDED JOBS. ENTERPRISE ZONES REPRESENT A REAL ECONOMIC PROMISE TO ECONOMICALLY DISTRESSED AREAS, SUCH AS THOSE IN MY OWN STATE OF ILLINOIS, AND ACROSS OUR NATION. WITH THE RIGHT PACKAGE OF REFORMS, IMPROVEMENTS, AND INCENTIVES, WE CAN ENSURE THAT THE POTENTIAL OF ENTERPRISE ZONES IS FULLY REALIZED.

AGAIN, I WELCOME THE DISTINGUISHED WITNESSES BEFORE US, AND LOOK FORWARD TO HEARING THEIR TESTIMONY. THANK YOU, MR. CHAIRMAN.

Senator LIEBERMAN. Thank you.
Senator Burns.

STATEMENT OF HON. CONRAD BURNS, A U.S. SENATOR FROM THE STATE OF MONTANA

Senator BURNS. Thank you, Mr. Chairman. I just have a short statement. I'm sorry I was just a wee bit late today.

We are very much aware today that the struggles of business—and this won't last too long. And, Secretary, it is nice to see you here. And I know you have championed this cause a long time just looking at the history of the thing.

The one shortcoming I think that we in the West—we fail to understand just exactly what is happening to our inner cities, in fact, our largest cities. And sometimes we do not appreciate enough what you are doing for those inner city areas.

So, I am here in support of you and what you are trying to do because I have a feeling that—I have always lived under the philosophy that if we help other folks help themselves, we solve a lot of our own problems along with it.

So, I am happy to be here—and your efforts and what you're trying to do. And I know you have your hands full down there. And I know you are down to 14 hour days now, and I can appreciate that.

Mr. Chairman, I appreciate your effort on this and the Ranking Member, Senator Boschwitz, and look forward to hearing from the Secretary on how we can help.

[The prepared statement of Senator Burns follows:]

SMALL BUSINESS ENTERPRISE ZONES

submitted by
Senator Conrad Burns

September 21, 1989

Mr. Chairman, I thank you for the opportunity to show my support today for Senate Bill 58.

We are all very much aware today of the struggles that still exist in our recovering economy. There many areas in this great country of ours that are just beginning to recuperate from the recession, my home state of Montana among them.

Therefore, it is with great interest that I support a move that would encourage the relocation of successful businesses to areas of our country that need an economical shot in the arm. The efforts of then Congressmen Kemp and Garcia in 1980 to introduce this positive movement was farsighted and to their credit. It is vision like theirs that will bring about the revitalization of rural and urban areas alike.

Small Businesses in this country continually need to be encouraged to grow. They are the business lifeblood of our American culture.

They not only provide jobs and products and services, they provide pride and independence in Americans, Americans we don't have to support on welfare.

Mr. Chairman, I am going to keep this short today and step aside to give more time to our distinguished guest Secretary Kemp. Mr. Secretary, it's good to see you here today. I would like to personally commend you on the job you are doing. I know it's not been an easy one. I certainly do appreciate all the help you have given my constituents this year. And I certainly look forward to working with you in the future.

Senator LIEBERMAN. Thank you, Senator Burns.

Senator Wallop, do you have an opening statement?

Senator WALLOP. Mr. Chairman, I do but I'll insert it in the record. It's neither illuminating nor stimulating. [Laughter.]

But it does welcome the Secretary and it also expresses great support for an idea which we have shared over a long period of time.

[The prepared statement of Senator Wallop follows:]

STATEMENT BY SENATOR MALCOLM WALLOP
BEFORE THE SENATE COMMITTEE ON SMALL BUSINESS
THE IMPACT OF ENTERPRISE ZONES ON SMALL BUSINESS
GROWTH AND DEVELOPMENT
THURSDAY, SEPTEMBER 21, 1989

Thank you, Mr. Chairman, for calling today's hearing on the enterprise zone program and its potential impact on small business growth and development. I am pleased that Secretary Kemp is here to testify and I look forward to hearing his views on the enterprise zone proposal recently put forth by the Administration. As a Senator from a rural state, I enthusiastically support the concept of enterprise zones in rural parts of America like Wyoming. I am eager to know how many of the proposed enterprise zones will be designated for rural areas.

As I pointed out in the hearing we held on this issue in June, I am not opposed to using the Tax Code to encourage investments and economic development. I do, however, have some reservations about adopting such limited tax incentives. For instance, I would note that the House Ways and Means Committee recently adopted a reduction in the capital gains tax which I believe will help spur investments in small entrepreneurial companies. As a cosponsor of legislation to cut the capital gains tax, I will urge the Senate Finance Committee to follow suit.

A reduction in the capital gains tax would enhance the ability of small businesses to obtain equity investments in their company, thus allowing them to expand their business, create new jobs and benefit a broader segment of our society. Wyoming has America's largest number of small businesses per capita. I believe they should be the primary focus of our economic development efforts, whether it be through enterprise zones or reducing the tax and regulatory burdens in order to help them prosper.

Again, let me say that I support the efforts of this Administration to revitalize urban and rural communities across the country. I look forward to the comments about that prospect and trust this hearing will provide a concrete basis for enacting enterprise zone legislation later this year.

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Senator BOSCHWITZ. I think the Senator should go right ahead. We heard a number of those. [Laughter.]

Including ones from me.

Senator LIEBERMAN. Senator Grassley, we want to welcome you to the Democratic side for this hearing. [Laughter.]

It's an indication of the bipartisan support for this concept.

Secretary KEMP. That's big news in Iowa. [Laughter.]

Senator GRASSLEY. That's the first time I really got your attention. [Laughter.]

Senator BOSCHWITZ. You are getting ours too I might say. [Laughter.]

Senator GRASSLEY. I'm just going to submit my statement for the record and welcome Secretary Kemp here. We know that he has a very tough job before him in the sense of all the administration of his department, and I know he came here to talk to us about other things today. But I wish him well, and I have every reason to believe he is going to succeed in straightening things out and getting things back on track.

[The prepared statement of Senator Grassley follows:]

STATEMENT BY SENATOR CHARLES E. GRASSLEY

MR. CHAIRMAN:

I THANK YOU AND THE RANKING MEMBER, SENATOR BOSCHWITZ FOR CONVENING THIS HEARING ON THE ISSUE OF ENTERPRIZE ZONES, WHICH, AS WE KNOW, ARE SPECIAL AREAS DESIGNATED TO ASSIST NEW BUSINESS DEVELOPMENT.

THE CONCEPT OF ENTERPRIZE ZONES HAS BEEN DEBATED FOR AT LEAST THE LAST NINE YEARS SINCE FORMER CONGRESSMAN--NOW SECRETARY KEMP, ALONG WITH CONGRESSMAN GARCIA, INITIATED LEGISLATION ON THE MATTER.

AS WE ALL KNOW, CONGRESS PASSED THE FEDERAL ENTERPRISE PROGRAM IN 1987. HOWEVER, THIS PROGRAM IS BASED ON VOLUNTARY INITIATIVES ON THE PART OF CERTAIN AGENCIES, AND DID NOT INCLUDE ANY BENEFICIAL TAX PROVISIONS.

THE LATEST ATTEMPT AT PURSUING ENTERPRISE ZONE LEGISLATION TOOK PLACE RECENTLY WHEN CONGRESSMAN SCHULZE TRIED TO INCLUDE AN ENTERPRISE ZONE PROPOSAL IN THE WAYS AND MEANS BUDGET RECONCILIATION BILL. UNFORTUNATELY, CONGRESSMAN SCHULZE WAS UNSUCCESSFUL.

MY OWN STATE OF IOWA IS SERIOUSLY LOOKING INTO THE DEVELOPMENT OF AN ENTERPRISE ZONE PROGRAM, AND WOULD LIKE TO SEE MORE DIRECTION ON THE FEDERAL LEVEL.

I, THEREFORE, LOOK FORWARD TO THE TESTIMONY OF TODAY'S WITNESSES AS WE CONTINUE OUR CONSIDERATION OF ENTERPRISE ZONES AND THEIR EFFECT ON IMPROVING THE AMERICAN ECONOMY.

Secretary KEMP. Thank you.

Senator LIEBERMAN. Mr. Secretary, there is no need for any further introduction. We are all obviously very glad you are here, very appreciative of your support of this concept and look forward to hearing you now.

STATEMENT OF HON. JACK KEMP, SECRETARY OF HOUSING AND URBAN DEVELOPMENT, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, WASHINGTON, DC, ACCOMPANIED BY MARY BRUNETTE, SPECIAL ASSISTANT TO THE SECRETARY FOR POLICY DEVELOPMENT AND COMMUNICATIONS, AND THOMAS HUMBERT, DEPUTY ASSISTANT SECRETARY FOR POLICY DEVELOPMENT

Secretary KEMP. Mr. Chairman, thank you and to you, Joe, and Rudy and to Senator Bumpers and each and every Member of the Committee and to the friendly comments on both sides of the aisle. I appreciate it personally and I certainly appreciate the kind words for our efforts to really celebrate, if you will, the 25th anniversary of the war on poverty with a real anti-poverty tool. It is not the only tool, but it is one of many that ought to be used. And I very much appreciate the hospitality of this Committee, appreciate your leadership and that of Senator Boschwitz and each and every Member sitting around the table.

I think I have visited just about every State, and if I have not yet, I certainly will be doing that. Montana, Wyoming, and Missouri are close on the heels of visits along with Wisconsin and Minnesota. That will teach me to start mentioning States. But I have appreciated the opportunity to visit firsthand many of those urban and rural pockets of poverty.

Let me just say that I would like to submit my testimony for the record. I do not even need to read it anymore. It comes out of the marrow of my bones I've been doing it for so long. And you reminded me, Rudy and Joe and Bob and everybody else, that we started this back in 1979. Jimmy Carter was President. It had Democratic support, Republican support. Mrs. Thatcher has used Enterprise Zones. The State of Israel has used Enterprise Zones. There are Enterprise Zones in Singapore and Hong Kong and Asia and Latin America and India. Some work, some don't. Some are dramatic, some are not so dramatic. Some are basically perhaps spending oriented, some are tax driven.

But, Mr. Chairman, you pointed out in your quote of President Kennedy that growth was like the weather. Everybody talked about it. Nobody has done anything about it. I give John F. Kennedy a lot of credit for a spectacular economic recovery without inflation in the 1960s. And it is no secret that some of my Republican friends want to take a little bit of credit for the macroeconomic recovery and some of the good that has happened in the last six or 7 years. But it is not Republican or Democrat. You mentioned President Kennedy, and I could mention Kemp, Roth, Kasten, Boschwitz, and so forth.

But the most important thing is we need to extend growth into those pockets of poverty, urban and rural, that have been left out of the macro-recovery.

And it seems to me that as we look at this, the 25th anniversary of the war on poverty, as we look at what we can do today, as we look at what passed the Ways and Means Committee, as we look at the opportunity the Senate has on the floor and in Committee to do something that goes beyond what was done in the Ways and Means Committee, Mr. Chairman, it seems to me that this would be a propitious time.

I hope you feel, as I think is reflected in this Committee, a sense of urgency about the fact that, as Mr. Kasten pointed out, drugs are not just a criminal activity. It is criminal, but in a sense there is despair. We have seen it all over this country.

Senator Dixon has been one of the champions of the idea of giving people in public housing a chance to manage and control and homestead in public housing. I was in Chicago the other day at Rockwell Gardens. What a thrill, Senator Dixon, to see the progress that has been made in Chicago, Democrat and Republican alike, black and white, to clean out, move forward. Mr. Woodson who will be testifying later, and your name always comes up when we are with public housing residents, Senator Dixon, because you have helped to champion that cause. And I am a Secretary of Housing who thinks that is just an essential ingredient.

Senator Kerry and I were together in Lowell and other parts of Massachusetts, and it was amazing how many things we found to talk about and agree upon. And I do not need to tell my colleagues on the right how much I appreciate their friendship.

There is a big debate over capital gains. I happen to be for eliminating it some day, and President Bush wants to bring it to 15. And that debate will go on, and it has become partisan for which I am disappointed. But, nonetheless, I would make one point.

The Capital Gains Tax is not a tax on old wealth as much as it's a tax on new wealth. But irrespective of the debate over capital gains and revenues and the impact on the budget and the impact on venture capital markets and the impact on savings and the impact on trying to reduce the double and triple taxation of income that occurs in this country and all of the macro and micro statistics, there ought to be one thing upon which Democrat and Republican, liberal and conservative, black and white, urban and rural Americans agree upon, that we cannot in a rising economy leave people behind. We cannot leave behind pockets of incredible poverty and grinding, abject despair that I have seen and that each and every one of us have seen.

And I would hope that in the opportunity that is going to soon be coming to the Senate, that in the reconciliation package for a very modest investment—for a very modest investment—let me say parenthetically the geothermal tax credit is I think $44 million of so-called lost revenue. The first year of an Enterprise Zone for 15 zones to get it started as a demonstration project leading to 50 or 75 or even more in the future—the first year, 1990 fiscal year would be $50 million.

Now, I am not against the geothermal tax credit if that's what the Congress decides it wants to do, to encourage that investment. And I am not against solar power energy development, if the Congress sees in its wisdom that it wants to put an incentive in there for investment in solar power.

But it seems to me for a modest investment, Mr. Chairman, you have the opportunity on the floor of the Senate and in this Committee to strike a blow for people who think they are being left out, left behind. They see corporations get tax incentives. They see people on levels of income far above them get what they perceive to be a particular benefit in the tax code. And we are leaving the potential of our inner cities and rural pockets of poverty out of this equation.

And it assumes that we sit up in judgment on poor people and suggest that there are no entrepreneurs among minority people or poor people. And I think it is demonstrably self-evident in the last several years, whether it is right here in Washington, DC, at Kenilworth Park or Chicago or in Boston or in any one of our States, that poor people, if given the opportunity, can be empowered, can be trusted, can become entrepreneurs. There are some amazing stories, and Mr. Butler and Bob Woodson will go into that at greater detail.

But I think that I want to go back to something you said, Joe. John Kennedy made also another great statement. He said, "People respond to rewards. The whole theory behind the early 1960 tax rate reductions and reforms were predicated upon his belief that people would respond. And I believe with all my heart that if you put a strong enough carrot, a strong enough incentive, a strong enough and dramatic enough climate for small businessmen and businesswomen to form capital and to take risks and to start businesses and to grow and build up an estate and maybe leave it to their children or give their children an education, I think that we must not forget that minorities and low income peoples in urban and rural America and on the reservations of Native Americans ought to have the same opportunity as Wall Street and Main Street of our major cities and towns and villages.

So, I am not going into all of the details of the bill. Generally it eliminates the capital gains in a green-lined area that we decide by competition, Mr. Chairman.

I hope you saw my headline the other day in the New York Times and the Washington Post that the Secretary wants to remove all discretion from the headquarters of HUD. I am not looking to make decisions based on politics. I am not looking to make decisions based upon who knows who at HUD or who knows who in the Republican or the Democratic Party. I pledge to you, Mr. Chairman, and to each of my colleagues we are going to make that place work for low income people, low income communities, be they rural or urban I would say to the Senator from Montana and other rural areas of America, but I want you to know we are not going to use discretion.

So, we want a competitive process in Enterprise Zones. And we want to look based upon those criteria in which we can objectively demonstrate such a need, a profound need. And we are willing to put some compensatory tax initiatives and incentives into that area. So, we want to be competitive, obviously.

We want Mayors and Governors to take steps themselves. You, Mr. Chairman, in Connecticut, as you said, it isn't working in Connecticut. Tom Kean, the Governor of New Jersey, said that for every dollar invested in an Enterprise Zone in New Jersey—and I

think there are 10 at last count in New Jersey—it delivers $5 of revenues to the State and to the cities of New Jersey for the dollar of invested tax incentive, if you will.

They are working in California, Illinois to a lesser extent, but I would make the case, Senator Dixon, that the incentives are not great enough. New York has them. Mario Cuomo calls them opportunity zones. I have called them Enterprise Zones. Mrs. Thatcher calls them something else, but in Docklands of London there has been a remarkable turnaround of the inner City of London predicated upon an Enterprise Zone. Governor Luis Munoz Marin, one of the great Governors of the Caribbean, of Puerto Rico, used an Enterprise Zone to create Operation Bootstrap.

We need to eliminate the capital gains tax in these areas.

Senator Kerry has talked about a revolving loan fund and without specifically addressing that, I too am concerned about that, as was Congressman Rangel of Harlem with whom I visited in Harlem 2 weeks ago. And he suggested that we ought to have an immediate expensing of investment in the equity or the debenture of an Enterprise Zone in a minority or green-lined community. It is in the bill. You can write off in the first year or expense $50,000 of invested capital into that green-lined area of a zone, be it urban or rural.

And, of course, the woman or the man that takes a job, moves from welfare to the job, faces as we all know a terrible disincentive because as you take a job from welfare and unemployment, your welfare and unemployment, nontaxable source of revenue, goes down and the tax on payroll and the tax on income goes up.

And I do not know if this is true throughout the country, but I have heard that there are statistics that show that right here in Washington, DC, if a woman on welfare with two children were to take a job, she would have to earn $16,000 or $17,000 or $18,000 of pretax income in the job on the first rung of that ladder to get the equivalent of $9,000 or $10,000 of transfer payment income which is not taxed. So, we have a disincentive.

Now, some say abolish welfare. And I do not think in our society, that there is anyone who wants to abolish a net under which people should not be allowed to fall irrespective over the debate over how high that net should be. The Enterprise Zone bill says that there is not going to be any tax on her income or his income as they move from welfare and unemployment into the ladder of opportunity upon which we want all Americans irrespective of color, race, creed or condition to climb.

And so, it is in that spirit, Senator Lieberman, and to you, Rudy, and Bob and each and every one of you who I think have a magnificent opportunity at this moment when that bill comes over here to act on behalf of those who feel forgotten, who some think are least and last and lost, but who deserve the same opportunity to become entrepreneurs and to get jobs and to climb that ladder as we want for children and minorities and middle income Americans who live in other parts more affluent throughout our Nation.

So, I appreciate your hospitality. I appreciate the leadership in this Committee, and look forward to working with you in any way I can to make sure that this bill comes to the floor and gets a chance to be voted up or down. And I would trust the wisdom of the Senate on an up or down vote on Enterprise Zones.

[The prepared statement of Secretary Kemp follows:]

Testimony of Secretary Jack Kemp
on Enterprise Zones Before the
Senate Committee on Small Business
-September 21, 1989

ENTERPRISE ZONES -- RESTORING HOPE TO AMERICA'S INNER CITIES

Chairman Bumpers, Senator Boschwitz, Senator Lieberman and members of the Committee, it is a pleasure to appear before you today on the topic of revitalizing our inner cities, rural areas, and Indian communities a subject that is not only of critical interest to this Committee but a high priority of President Bush and mine as well.

President Bush and I are committed to economic development and jobs through enterprise zones to encourage entrepreneurship and job creation in distressed inner cities and rural areas. The President has recommended enterprise zones in his budget, and he has forwarded his proposals to Congress which includes the elements we consider critical to success. I commend Senator Boschwitz, Senator Danforth, and Senator John McCain for their support of the enterprise zones concept. I intend to work closely with Congress on a comprehensive package of incentives for every area in America that seeks growth and opportunity whether in rural, urban, or Indian communities.

The Ways and Means Committee just reported a tax bill that would reduce the capital gains tax. While I am a champion of the reduction in the capital gains tax rate for the Nation, I believe it would be a tragic and unfair mistake not to match this reduction with a dramatic package of economic incentives to revitalize inner city and poverty areas.

Unfortunately, the Ways and Means Committee ignored enterprise zones. Yet, they did find time and resources to report tax breaks accumulating over the next 5 years to $115 million for geothermal tax credits, $4.4 billion for the research and development tax credit, $3.2 billion for simplification of the corporate minimum tax, and $175 million for passive losses in the timber industry among others.

Mr. Chairman, these provisions are not necessarily bad. But, in my view, this reconciliation bill sadly misplaces our priorities. At a time when our Nation suffers from poverty, despair, and hopelessness in cities and rural areas across America, it would be unconscionable to ignore our Nation's poor, while providing assistance to business, energy, and prosperous Americans.

I hope that the Senate Finance Committee will rectify this mistake by reporting a strong Enterprise Zone bill this year. Enterprise Zones have been publicly debated for 10 years; it has been passed twice by the Senate. It's time to make it reality this year as part of the reconciliation tax package.

It is legitimate to ask how to pay for the cost of Enterprise Zones. I've always believed, of course, that Enterprise Zones will actually raise Federal tax revenues by stimulating economic activity and jobs. But even assuming "static" revenue estimates, the U.S. Department of Treasury has told the Ways and Means Committee that Enterprise Zones should be paid from the revenue gains arising from the capital gains tax reduction. Well, the Committee rightly passed the capital gains tax cut, but they forgot the Enterprise Zone bill that was supposed to go along with it.

Mr. Chairman, I am a strong supporter of the capital gains rate reduction. In 1963, John F. Kennedy proposed a capital gains reduction to 20 percent. "The tax on capital gains," he argued, "directly affects investment decisions, the mobility and flow of risk capital from static to more dymamic situations, the ease or difficulty experienced by new ventures in obtaining capital and thereby the strength and potential for growth of the economy."

If a capital gains tax cut did not help poor and middle income families, I would not be asking you to pass it today. As Secretary of Housing and Urban Development, however, I can tell you that average and low-income Americans have hundreds of billions of dollars in capital gains accrued in their homes, stock mutual funds and other assets. These average American families will directly benefit from a capital gains tax cut.

In reality, a dramatic reduction in the capital gains tax would help the inner city or rural poor in three ways:

First, hundreds of billions of dollars in assets would be unlocked from existing assets and freed to invest in new business enterprises. The Administration estimates that a reduction to 15 percent would boost realized capital gains by 91 percent in FY 1991 to a total of $349 billion. Those sales would give the enterprising poor and small business person an enormous leg up on access to new seed capital for business start ups or expansion. Much of this investment capital comes from "informal" investors--friends and relatives, for example--who are estimated by the SBA to account for a great amount of seed capital than organized venture capital firms.

Second, a lower capital gains tax rate increases the willingness of investors to take risks in small, precarious firms whose long term success is not at all guaranteed--in other words, exactly the type of firms that will likely start in depressed communities. A high capital gains tax rate reduces risktaking because capital gains are taxed while capital losses are not able to be deducted fully. Therefore, the government shares in the success, but not in the failure of a business.

Third, poor people who want to become entrepreneurs and small business people will be more likely to start a business if they believe that they will receive a greater share of the rewards of that effort. In fast-growing small enterprises, where you're starting from ground zero, capital gains are much more significant to the owner-manager than in big business where managers are disproportionately compensated through salary and bonuses.

Mr. Chairman, while the capital gains tax cut is important, it is critical that it be matched with the three major incentives contained in the Administration's Enterprise Zone bill.

As I mentioned, the first incentive in President Bush's Enterprise Zone initiative is a zero capital gains tax rate on tangible zone assets. President Bush and I are confident that this incentive can help "percolate" a whole new generation of small business entrepreneurs and community leaders, set in motion a process of self-improvement and job-generation, but most of all restore hope for progress in America's future.

Mr. Chairman, I think it is disappointing that there are fewer than 800,000 minority-owned businesses out of more than 12 million total. Minorities own less than 7 percent of the total business in America. I believe our Nation should target a goal of doubling or tripling the number of new minority-owned businesses by the end of this century.

When the top capital gains tax rate was reduced from 49 percent under previous law to 20 percent, the number of small company startups more than doubled, rising to 640,000 from 270,000, creating 15 million new jobs. By eliminating the capital gains tax in depressed areas, we can put that enormous job-creating potential to work exactly where it is needed most.

The second incentive is expensing of investor purchase of newly-issued small zone corporate stock. Because start up businesses typically have little or no tax liability in their first years, there is a limit to what direct tax reductions can do to help these firms. That's why the Administration proposes giving investors an upfront deduction for up to $50,000 per year of new equity investment, with a $250,000 lifetime limit. Expensing will be available for investment in corporations having less than $5 million of total assets, so long as the investments coincide with comparable increases in the corporation's tangible zone assets. Expensing is one of the most innovative and exciting features of the Administration's proposal.

In return for an up-front tax deduction, investors would provide inner city and rural entrepreneurs the kind of seed capital they need to start up retail stores, a printing shop, a delivery company, laundries, or workshops, just to name a few examples.

The initial revenue costs of equity expensing may be recouped eventually since the entire amount of the investment plus any net gain will be taxed as ordinary income at the time the enterprise zone stock is disposed of. Federal taxes would only be <u>deferred</u>, not eliminated.

The third incentive is a 5 percent refundable tax credit for the first $10,500 of wages to individuals working in a zone and having total wages below $20,000. The maximum credit will be $525, and the credit will phase out between $20,000 and $25,000 of total wages.

Welfare recipients and other low-income people on government support often face effective tax rates that are steeper than for our highest income earners. As they enter the workforce, not only do they pay income and social security taxes on the earnings, but they also face higher effective marginal taxes from losing their AFDC, food stamps, Medicaid coverage and other government payments cut as well as from new costs such as child care and other employment related expenses.

The Administration believes that giving employees greater incentives to leave welfare and take advantage of new job opportunities will help break the poverty trap.

The President's enterprise zone initiative will be available to workers and investors in up to 50 zones. The 50 zones will may be phased-in, 15 in 1990, 15 in 1991, 15 in 1992 and five in 1993. Zone designation will be based both on distress criteria and on State and local plans of action.

As I said before, my personal opinion is that enterprise zones in the long run will actually raise money. The Administration 's revenue estimates assume no change in levels of national economic activity as a result of enterprise zones. Using this methodology, the Administration's proposal will cost $1.04 billion over 4 years and $50 million in FY 1990, meeting the amount set-aside in the President's FY 1990 Budget. I might add that New Jersey's own enterprise zone program has created so much new economic activity in the zones that the program has been estimated to raise between $1.90 and $5.20 for every dollar of tax incentives they provided.

Competitive Selection

The Administration's Enterprise Zones initiative also recommends competitive designation for zones. Federal tax relief is only one component of a comprehensive urban and rural strategy. But Federal tax incentives can act as a catalyst for other State, local and private sector efforts to restore vitality and economic buoyancy. In a competitive process, those States and localities which offered the strongest package of incentives and initiatives would receive preferential selection for zone eligibility.

For example, some preference for Federal enterprise zone designation could be given to States and localities that offer relief from land use regulations, zoning laws, and real estate taxes, building codes and rent control. Similarly, States and localities could toughen community drug enforcement, begin new anti-crime efforts or improve municipal services and neighborhood infrastructure.

Questions About Enterprise Zones

I would like to discuss briefly four major questions about enterprise zones.

First, some people question whether zones will simply redistribute growth from outside the enterprise zone to inside the zone with no net increase in jobs or investment. I strongly believe that economic growth is not a zero sum proposition and that tax rate reductions on labor and capital create new growth, new jobs, and new investment. The 1981 and 1986 tax rate reductions, for example, helped generate 19 million new jobs, over 4 percent economic growth a year, and rapidly rising productivity. U.S. progress was not stolen from or at the expense of economic growth in the rest of the world. In fact, Americans bought record imports from the rest of the world, acting as the locomotive for world economic recovery.

Rather than "stealing" growth and business from outside the zone, I believe that zones will actually have positive effects on outlying communities. As retail and commercial business prosper in enterprise zones, business outside the zone will also prosper from the increasing customer base, the expanded employment and income growth in the area, and the improved community and business environment.

The second major question about enterprise zones is whether they really will help small business. We intentionally designed our tax incentives with small business in mind. For example, the elimination of the capital gains tax rate is only on new investment. We also know that small, fast growing firms are most stimulated by reductions in taxes on capital gains, witness the huge increase in small firms following the last capital gains tax cut. Our expensing provision is also limited to firms with total assets of less than $5 million. Again, only small and medium size firm will benefit. The income tax credit is for low income workers.

The third major concern is whether our tax incentives will create possibilities for abuses and uneconomic tax sheltering and asset churning.

We have protected against such abuses by careful crafting of our tax incentives, as well as recommending regulations which should prevent remaining problems.

Substantially all the activity of qualified corporations enjoying our tax incentives must be located in the zones. We will require that most employees of enterprise zone firms be in a zone, and most of the equipment owned by an enterprise firm be in the zone.

Unprofitable enterprises also will not be kept in business simply as a result of our tax incentives. Equity expensing is only a deferral of taxes. The investor certainly knows that he or she will have to pay taxes on the equity investment when it is sold and therefore investment decisions are not distorted. Similarly, the capital gains tax reduction is not a subsidy. Capital gains taxation is a second or double tax on corporate income. Eliminating this tax does not distort investment decisions, but moves the tax code toward more neutral taxation of capital income.

No opportunity will exist for unfair tax sheltering for the rich. Our up front expensing provision is limited to $50,000 annually per investor, with a $250,000 lifetime limit. Like the low income housing tax credit, this incentive is designed to bring capital to socially-useful purposes without allowing upper-income people to escape taxes. Plus, the expensing provision is only a deferral of taxes, like an IRA, not an elimination of taxes.

In short, our tax incentives will not cause companies to start in zones that otherwise would be uneconomic and unprofitable. We have taken every precaution to make sure that enterprise zones will expand indigenous economic growth, without causing new avenues for more tax sheltering of the rich, sham economic activities, or reshuffling of economic activity.

Another criticism of enterprise zones can also be put to rest. Let me assure you that I do not consider enterprise zones to be a replacement for other Federal programs, although I think that over time, as enterprise zones succeed, we may well see them more efficiently accomplishing the goals of many Federal programs. I view enterprise zones as one major weapon in the arsenal of our war on poverty. It is a way to bring together the resources of all levels of government and the private sector in a productive partnership.

Members of the Committee, I believe we are forging a common and bi-partisan agenda for waging a new and successful war on poverty. Our principles are founded on our faith in our democratic capitalist system, but our inspiration comes from Dr. Martin Luther King, who said he had faith in America and an audacious faith in the future of mankind.

Through enterprise zones we can continue this new war on poverty, and one that is successful, where jobs, homes, and hope replace despair and unemployment.

Thank you for this opportunity to present the Administration's view of enterprise zones. I am happy to respond to your questions.

Enterprise Zones

Background

The revitalization of urban areas has been a Federal government priority for a long time. This has been exemplified by the establishment of Urban Renewal programs in the 50's and 60's to the UDAG and CDBG programs of the seventies and eighties. Following in this tradition, enterprise zones were brought to this country in the late seventies from England as a way to revitalize distressed urban communities by using the tax system rather than direct cash aid. This concept was immediately embraced by conservatives in Congress. The idea is centered around providing tax incentives as well as regulatory relief to businesses that locate in communities designated as enterprise zones. The anticipated result would be job creation-- particularly for the disadvantaged worker and the hard core unemployed.

It was assumed the concept had broad based political support when, in 1978, conservative Congressman Jack Kemp and liberal Congressman Bob Garcia introduced legislation that would have given Federal tax incentives to businesses located in areas designated as enterprise zones. This assumption was wrong. Partisan politics has been the downfall of enterprise zone legislation for the past ten years. Fearing the experiment might work, liberals were not going to give conservatives credit for revitalizing cities.

It was not until the "Housing and Community Development Act of 1987" that Congress gave the Federal government authority to designate areas as enterprise zones. However, the major enticement, Federal tax relief, was not included in the legislation. Critics contend that it would cost the IRS about $2 billion in lost revenue.

Most enterprise zone activity has occurred on the state and local level. States have taken it upon themselves to promote and experiment with the program. To date 36 states have enacted some form of enterprise zone legislation. Most offer tax incentives, through credits or exemptions, to businesses that locate in enterprise zones and hire certain percentages of workers who live in those areas. Some states provide referral services to employers as well as other support services.

- In 1983, the Illinois EZ program provided incentives that have saved 2,000 jobs and stimulated $23 million in new investment.

- EZs in Topeka, Kansas have encouraged the creation of up to 600 jobs and new investment commitments of over $80 million.

- Louisiana and Florida have calculated that for every $1.00 revenue loss between $1.40 and $1.55 have been gained through increased tax revenues and/or reductions in the high costs of unemployment.

How it Works

For Federal legislation requires, states and/or local governments to undertake at least four of the following six actions:

- Reduce tax rates or fees applying within the zone.
- Reduce, remove, simplify, streamline paperwork.
- Have public authorities or private entities become involved in the program (including commitment to provide jobs, job training, and technical, financial, or other assistance).
- Give preference to minority contractors.
- Donate real estate to neighborhood organizations agreeing to operate a business on the land.
- Increase the level of efficiency of public services.

These actions can be funded by any program administered by HUD or the Dept. of Agriculture.

NCNE Policy Recommendations

NCNE supports the concept of enterprise zones as a way to revitalize distressed inner city communities. We would also like to see tax incentives that would make capital available to people who live in EZs who want to own and operate their own businesses.

- One such proposal would involve allowing people who make such investments to write them off their taxes immediately as a business loss. This is similar to the tax treatment of "Section 1244" stock.

NCNE is not only concerned with job creation in inner city neighborhoods but also with wealth creation, which results from the formation of businesses, as a way to achieve economic revitalization and self-sufficiency.

RESPONSES TO QUESTIONS SUBMITTED
BY SENATOR MALCOLM WALLOP

Q. How do you plan on making a distinction between urban and rural enterprise zones?

A. We propose that the rural set-aside apply to zones within communities which are either under 50,000 population, or outside a Metropolitan Statistical Area.

Q. If you make such a distinction, what is the potential for creating them in rural state like Wyoming which has no state income tax and no corporate tax?

A. We believe that the potential is very good. Several state enterprise zone programs include provisions for rural zones, and many of these have been quite successful. Because of the relatively isolated nature of rural areas, zones in these regions tend to focus on business and job retention, expansion, and job creation, rather than on industry attraction.

Q. Now that some states have done limited experiments with enterprise zones, can you tell me how an enterprise zone might further influence a small business person's decision to start a new business, particularly if he or she is already inclined to do so?

A. The primary influences on small business would be the potential for reducing the cost of labor and capital, increasing the availability of start-up capital, and increasing the potential reward of risk-taking.

Q. Why would the incentives offered for an enterprise zone benefit our society as a whole more than a general tax reduction across the board?

A. I am strong supporter of general reductions in tax rates as a stimulus to economic growth. But, there are areas of the country which have not risen with the economic tide and require special incentives to stimulate economic development. The President's enterprise zone tax incentives have been carefully crafted to encourage entrepreneurship in these distressed areas. These incentives have the potential for leveraging a great deal of private investment and job creation in these areas.

Q. **What do you estimate the cost of that package to be and have you weighed that cost against the potential for small business growth and development?**

A. The estimated tax expenditure for the first four years of the program is $1.05 billion. But I don't believe that enterprise zones will actually lose a cent. In fact, the stronger economic growth and lower government outlays should raise revenue and reduce the budget deficit. We need to take into account fully the offsetting benefits such as taking people off of welfare, reducing aid to dependent children and food stamp outlays, and putting paychecks into a depressed local economy.

Senator LIEBERMAN. Thank you, Mr. Chairman. I appreciate your being here.

Let me say I understand that you have to be somewhere else at 2:30. So, maybe you have a little more than a ½ hour. And as a result, we will go around with some questions, but we will each try not to take too much of your time.

Do I hear you to say that what you are asking us is to consider perhaps amending the reconciliation bill with Enterprise Zone legislation when it comes over here?

Secretary KEMP. I guess I am looking, Mr. Chairman, for any vehicle that we can possibly find. I cannot hide my disappointment over the fact that the Ways and Means Committee took up Solar Tax Credits and Geothermal Tax Credits and Corporate Tax Credits and left behind the impoverished areas of the country.

It is no secret if you listen to John Jacob of the Urban League tell us in his "State of Black America" that out of 13.1 million small businessmen and businesswomen in America, there are only 350,000 black-owned businesses, only 340,000 Hispanic-owned businesses. We have to do something to put some incentive back into those communities. And I think this is a good start.

Senator LIEBERMAN. You raise this procedural possibility because of your own sense of urgency about this. In other words, let's——

Secretary KEMP. Well, having been in the inner cities, it just strikes me that unemployment among minority youth is in the 30 to 40 percent range. Unemployment among black heads of household is in the high teens. Women, minorities, the lack of minority ownership—another example, 13.1 percent of the American people happen to be black. Black-owned wealth in America is less than 1 percent of the total gross national product. It was higher in the depression. It was higher in reconstruction.

Hispanic and Asian and black and female and Native American—I just think there are many people who would like to become entrepreneurs, but the system is geared against their ability to create wealth, to accumulate an estate, and be able to build something for their own future. And that is the theory—and I believe it would be the practice—that would be manifest as it has in Missouri and has in other States.

Senator LIEBERMAN. The bill that Senator Boschwitz and I have introduced has substantially more in the way of benefits for activity in Enterprise Zones than the Administration bill. Would you talk about that a little bit? Do you think the administration bill does as much as we should be doing right now?

Secretary KEMP. Well, if it were up to you and me, Mr. Chairman, we would be far more audacious.

Senator LIEBERMAN. And Rudy.

Secretary KEMP. And Rudy and I think all of us. We are in a period where the budget has become almost the sole criterion by which we make a judgment about our economy. I am disappointed in that, but of course I have a minority view of my own about what is driving the deficit.

But as I pointed out, it seems to me that this is a good start. It is a good demonstration of what entrepreneurship can do in low income communities, and I think we ought to get started on it. And then after 1 or 2 years, we can take a look at the incentives, take a

look at the areas of the country, and hopefully some day we will have an Enterprise Zone from sea to shining sea. But we ought to get started, and this is a darned good start that the Bush Administration has proposed.

Senator LIEBERMAN. I have a lot more questions, but let me give some others the opportunity to get involved. Senator Boschwitz.

Senator BOSCHWITZ. Well, Mr. Chairman, you made the statement that I was going to make, that the President's bill is somewhat restrictive in what it wants to do. But, nevertheless, it is a good start. I would agree with the Secretary that it is a good start, allowing a Capital Gains exclusion, an outright deduction for an investment, and an employee credit, as the Secretary says, that would make replacement of welfare a little bit easier to achieve.

I wonder, Mr. Secretary—you have alluded to a number of Enterprise Zones that exist—if you could tell us where you think they have done the best and what should States do, or local communities? How can they supplement the bill that we would enact here?

Secretary KEMP. I understand from Senator Lieberman that there are 38 States with Enterprise Zones. It was my understanding that there were perhaps a few less, but if it is 38, that is a significant number of States. Some have very dramatic incentives, at least as far as States can provide. Others have far less.

GAO did a study in Maryland and they found out that it wasn't working. The reason it wasn't working is there was no carrot.

As Senator Bond pointed out earlier, in Missouri in St. Louis, they had a rather dramatic zone, at least for a State operated zone, and it was working, as Senator Bond pointed out. Tom Kean, the Governor of New Jersey, has been a strong proponent of Enterprise Zones.

Senator BOSCHWITZ. That five for one that you mentioned with respect to Governor Kean——

Secretary KEMP. Right, revenues.

Senator BOSCHWITZ. The revenues. Over what period of time did it take?

Secretary KEMP. We believe that when we got the numbers and the figures from Governor Kean, that that was over the period of the passage of the zones in New Jersey which are probably 4 or 5 years old.

Senator BOSCHWITZ. Already in other words.

Secretary KEMP. The report came out in May, right.

Senator BOSCHWITZ. They have already gotten a return, a five to one return, within the first 4 or 5 years.

Secretary KEMP. Well, the weakest zones returned about $1½ for every dollar of investment or maybe a little bit more, but the stronger zones, where there had been a greater incentive, there was a $5 payoff for every dollar of invested capital.

My point is in debating static budget numbers, I have been saying that if it does not work, it will not cost us anything. I mean, if no one does anything, economically it can't possibly cost anything. If it works and someone locates or starts a business that had no chance of ever having a business in the first place and hires one man or woman off the welfare roll, you are going to get a revenue feedback. It may not be to the Federal Government for a while, but it may be to the State and to the local government.

I got an interesting statistic the other day where New York City announced that they lost $2.5 billion from capital gains. Well, it was the capital gains revenues that they expected to get when the rates were lower, and they lost revenue when the rates went up.

I am a great believer, although I am subject to a lot of criticism on this point, that a lower capital gains tax will lead to higher revenue not only for the Feds, but also for the City of New York and New Jersey, the northeast quadrant of the United States, anyplace where you want to stimulate economic activity. But, of course, these are perhaps subjective opinions.

But I do believe that we would get a payoff in terms of putting some hope and opportunity back into areas where people feel like they have been left out of the macroeconomic recovery that we have enjoyed for the last 6 years.

Senator LIEBERMAN. Senator Boschwitz has gone to the floor to participate in a vote. Rather than recessing the hearing, we are going to see if we can do our voting in shifts so we take full advantage of your limited time.

Senator Kerry, do you have questions?

Senator KERRY. Just very quickly, if I can.

Mr. Secretary, I would like to ask you if you could respond to the initial concept that I suggested regarding the drug designations. I mean, obviously, if there is a designation of a high intensity area, it is a reflection of the despair, degradation, and so forth, that you referred to. Do you think the linkage to an automatic designation of an Enterprise Zone would be helpful and, in fact, even appropriate?

Secretary KEMP. I would be very interested in that, Senator Kerry. I would like to know how many zones are they considering, and then I would be subject to suggesting that we are going far beyond the Administration and the Budget Committee's original estimation that 50 zones would cost $1 billion over 4 years.

Had we said that every single, high intensive, at-risk community in the United States would automatically acquire an Enterprise Zone or a free-trade zone, there would be some budget consequences that would have to be taken into consideration.

But you are talking to at least one of the architects of the idea who would be willing, obviously, to work with you and this Committee to make sure we get as many into the process as possible. I think it's a great idea.

Senator KERRY. It may be that there will be a coincidence anyway of those areas that would automatically be designated, but I think we ought to keep that at the forefront of our approach.

Secretary KEMP. I would not be surprised at all, Senator Kerry, and I very much appreciate the very thoughtful suggestion that you have made.

And Senator Kasten made an equally important point that the drug effort cannot be combated only on building jails and prisons and more reform of our criminal justice system. We have to provide alternatives to those little boys on 71st and 15th Street that I saw the other day in Miami who were lined up on every single block for about 10 blocks as almost like the farmers' market on Fairfax Avenue in Los Angeles where I grew up who were hawking their wares, and they are in their low teens and even younger. And

it is a crime. We have to give them some legal options to the illicit trade in the so-called drug market.

Senator KERRY. Along those lines, as Chairman of the Urban and Minority Business Development Subcommittee of this Committee, I had a concern with a number of different aspects of both the 8(a) and the set-asides and all those kinds of programs.

One of the things that I am going to be suggesting is the creation of an Enterprise Zone Development Corps, which builds on the spirit of volunteerism that I think the President has appropriately tried to tap and which we should, and solicits from the professional communities, particularly from construction and labor and other areas, and also from managerial and corporate areas, people who would volunteer their technical and entrepreneurial experience within an Enterprise Zone perhaps for a year's basis, perhaps ongoing if they get excited, which one would hope they would.

Do you think that that approach would be helpful, and does it perhaps need the addition of, again, the reward that you talk about? Do you need some sort of a personal tax credit, or do you need a corporate credit or something? Or do you think you could create the corps without the reward?

Secretary KEMP. Let me say that the corps idea, getting men and women who have been successful in their business careers to take time as they have reached perhaps a level of their life in which they want to devote more of their time to some of these social ethologies that exist and economic problems that exist, is a great idea.

I do not think you would have to give them a credit. I do not think you would have to give them a tax benefit. I have not seen in my 19 years in public life, Senator Kerry, a time in which I found more men and women of success who would like to devote part of their income and capital investment and time to helping solve some of these so-called intractable problems as I have recently.

Last night at the dinner for Jim Rouse, that place was swarming with men and women of success who are putting time and effort and capital into nonprofit organizations. Mr. Woodson is finding the same thing as he travels the country.

And so, I think your idea is terrific. It is like a teacher corps. An entrepreneurial corps would be great because think of all the successful people in this country who would like to help minority-owned businessmen and businesswomen take advantage of a new climate.

But we have to put some teeth into the bill. And the reason I didn't designate the 200 or so Enterprise Zones that I was authorized to do in the last Housing Act was because why tell people that we are going to designate someplace an Enterprise Zone and then not have any incentive in there. But I think the incentive for a man or woman to take time off and help others is already there. It comes from a desire to be of assistance to the poor.

Senator KERRY. Let me just say, Mr. Secretary, I am delighted with your response. And I think that in the wake of the Richmond-Crowson decision, we are obviously going to have to be creative and thoughtful about how we protect access. And the set-aside concept is clearly going to be under test. So, we are going to have to find as many ways as we can to attract minorities into the business and to share in that.

The final comment I would make is I just want to say how refreshing it is—I think it is good politics as well as good sense, but no matter what it is, it is very refreshing to hear the Secretary of HUD and the Administration talking about those who are left behind and really laying on the table the first proposal that we have had actively in a long time to try to deal with it. And I think you know I share a belief that it isn't enough. That is not your fault or our fault because there is so much to do. But it certainly is more than we have been doing. And I think it is terrific that you are doing it, and I congratulate you for it.

Secretary KEMP. Thank you very much.

Senator LIEBERMAN. Amen. I agree with you, incidentally, in not having designated those 200 because there wasn't anything there. To me the remarkable thing is that some of the State Enterprise Zones, such as the ones in Connecticut, have worked without what is the major incentive, which is Federal tax relief. So, if we get this in place, heaven knows what could happen.

Senator Kasten.

Senator WALLOP. Mr. Chairman, we have five bells on and the Secretary has to go out. I just want to say, Jack, how much a pleasure it is to hear you and observe once again the incredible enthusiasm you bring to the work of Americans.

Secretary KEMP. Thank you.

Senator WALLOP. I won't be here to ask questions, but I know what the answers would be. [Laughter.]

Secretary KEMP. I was going to tell you we were thinking of putting a strategic defense initiative under every——[Laughter.]

Senator WALLOP. Give it a little incentive and away we go [Laughter.]

Secretary KEMP. It won't be a complete umbrella. [Laughter.]

Senator LIEBERMAN. Senator Kasten.

Senator KASTEN. Jack, I want to just—and I might have to leave before you finish your answer. But I want to get on the record the problems that we have had. As long as some of us have worked together on these different kinds of issues, we have had problems with Treasury, OMB, and all the different kinds of estimators around this town for the last 8 or 9 years. And yet, we still get the wrong kinds of estimates coming from the people that are on the policy side and we have to go out and get Chase Econometrics or somebody else in order to tell us what really happens.

The problem that you're running into, I am told, as we look to cosponsor these bills and work them through is that they are too expensive. Now, in your example for New Jersey, not one of them was too expensive. The only question was how much money each one of them made. And if you start to look at the real world, business growth, more tax dollars; more investment, more tax dollars; more jobs, more tax dollars; more income from Enterprise Zones, all of these are more tax revenue.

And in addition—and you talked about it briefly—we are taking people who are now tax users on welfare and different kinds of Government payments, unemployment compensation, trade adjustment assistance, whatever it might be, and turning them into workers, more tax dollars. And yet, we are not getting either from Joint Tax or Treasury that kind of dynamic work that we need in

order to make the point which everyone in this room I believe knows is true.

In this battle—now you are on the other side of the table. Now you are in the cabinet. You are an influential member of the cabinet. What can we do to start to get this Government, this Administration, to recognize that we are not playing in a static, but instead a dynamic, growth oriented, job creation kind of an atmosphere?

Secretary KEMP. Well, I think if it were purely objective, we would win the debate. I think the politics of envy is introduced by those who want to divide America between rich and poor. And I think it is an elitist attitude. I think once people see the poor as the enemy of the rich or vice versa, they begin to look at poverty as a perpetual condition.

And what I appreciate about this Committee and the statements that have been made here today on both sides of the aisle, we all agree that poverty is not a perpetual condition. Jesse Jackson said he was born in poverty, but poverty was not born in him. That is a human, not a necessarily class distinction. And changing attitudes is 90 percent of our lives. It's 95 percent of sports, and it's certainly 90 or 95 percent of business.

Bill Safire in the New York Times has an outstanding article on tax reform and talks about revenue feedback.

Pat Buchanan in the Washington Times a couple of days ago said that in 1979 under Jimmy Carter the top 5 percent of Americans paid 37 percent of all income taxes. By 1987 under Ronald Reagan, that had jumped to 43 percent.

Now, whether we like it or not, and no matter how it is said, wealthy Americans at lower rates are paying higher revenues into the Federal Treasury today than they were when the tax rates were at 70 or even 90 percent.

Senator KASTEN. Jack, I just want to interrupt.

I agree with that. My question is focused on this Administration and OMB, Treasury, Joint Tax. What can we do on our side of the table? You are now on a different side of the table than you have been as we work together. What can we do—I know Rudy shares this concern—to get our Administration to trot out dynamic estimates when we all know they are true?

I have about 2½ minutes to vote, and I'm going to run. But I'll come back and pick up on what you said through the transcript.

But this is the challenge I think in order to get these things through.

Secretary KEMP. I agree with you.

Senator KASTEN. I know Rudy shares my concern.

Secretary KEMP. Well, whether the green eyeshades in Treasury or OMB or in Congress or CBO—the President, George Bush, Dick Darman and Bob Kasten and Jack Kemp and a number of Democrats and Rudy Boschwitz are for it, so don't worry about the green eyeshades and the pencil.

Come back. [Laughter.]

Pass it and we'll get a test. There will be an empirical, objective——

Senator BOSCHWITZ. What were you reading from? Is that of recent vintage?

Secretary KEMP. This is Pat Buchanan's article in the Washington Times of 2 days ago. My article from the Post, Lighting Candles from Harlem to Watts, and an article by Bill Safire today in the New York Times. I've covered every major newspaper.

Senator BOSCHWITZ. I can't tell, Mr. Secretary, if you sound like a Member of the Administration or a Member of Congress. But I see that you are making the transition.

Secretary KEMP. I'm a congressman at large. [Laughter.]

Senator BOSCHWITZ. I like the bill that you have sent us. It doesn't include all the incentives that Senator Lieberman and I have put in our bills, but it does include one important incentive and that is a deduction that occurs even in the event there is not a profit.

Do you have a sense of which particular elements have been most successful on the statewide level or local level?

Secretary KEMP. I keep pointing to New Jersey primarily because we had the best revenue feedback from New Jersey that I have seen in the brief time that I have been at HUD. But sales tax, which was eliminated in New Jersey's Enterprise Zone or sharply reduced, had an impact on small businesses. There is not much that a State can do other than——

Senator BOSCHWITZ. The sales tax that they paid to——

Secretary KEMP. The sales tax that——

Senator BOSCHWITZ. The customer paid or that they paid in making acquisitions?

Secretary KEMP. Both actually, business and the consumer.

I met with the Democratic Mayor of Newark, Mayor Sharp James. He is an incredible supporter of Enterprise Zones. Talk to Mayors. They are supporters.

And I have always wondered, Rudy, why it is trickle down economics to lower a tax rate on an entrepreneur or on an investor or a venture capitalist or even a worker to some, yet it is not trickle down economics to subsidize high definition TV or to subsidize builders and lawyers and consultants to hopefully build housing for low income people.

I mean, talk about trickle down economics. I can prove empirically that the ripoff of the poor in the housing programs exceeds by anyone's wildest imaginations that which was done by giving an incentive to someone to invest in a new enterprise from Silicon Valley, CA, to Minneapolis or inner cities of this country.

I think we are losing the rhetorical battle because we have given up the high moral ground that somehow those who want to subsidize businesses to create jobs are more concerned about the poor than those who want to unleash the entrepreneurial talent of the poor themselves.

And I think there is a sense of elitism, a sense of egalitarianism run amuck, and a real clash of envy in this thing. And it's too bad. I think it has to end.

And my contribution to it is to say that while our friends on the socialist side of these arguments talk about redistributing bread in the name of social justice, as Luis Munoz Marin, the Governor of Puerto Rico who was a socialist, said when he became Governor I had to stop thinking just about redistributing bread and start figuring out how to create some bakeries for my people. And Operation

Bootstrap really was the result of Luis Munoz Marin's and the Congress' tax incentives for the Island of Puerto Rico, incidentally, which is really in desperate need of our help—all of us.

Senator BOSCHWITZ. Because of the hurricane.

Secretary KEMP. Right.

Senator BOSCHWITZ. Well, Mr. Secretary, I know that at the very beginning of this you said that you had to be at a Resolution Trust Board meeting at 2:30.

Secretary KEMP. I'm going from here to a Housing meeting. Could I just say to you, Senator Boschwitz, it seems to me ironic, our friends who talk about affordable housing, as important as that is—and it is a very important issue—how can we have housing affordable if we do not create more economic opportunity for people to have a job with which to get an income so that they can afford to rent or buy a home? I think those of us who care about affordable housing and incentives in the tax code need to also elevate the idea of jobs and economic expansion in minority and low-income communities so people can begin to have the means by which to afford to buy and rent.

And I think they are inextricably linked together, jobs with housing and housing with jobs, and it is important that I make that point as I leave for the oversight board of the Resolution Trust Corporation where I was appointed by Congress to be concerned about low income community development and low income housing which I will be. But I also think this is a very important issue. I hope you can use your vast influence to get this thing passed in the Senate.

Senator BOSCHWITZ. Well, I will try to use that vast influence. [Laughter.]

As you know, we have passed it in the Senate a couple of times and it was dropped in conference—a couple of bills that I authored, as a matter of fact. [Laughter.]

Listening to you is always energizing and, indeed, listening to you is inspirational. Your days spent in the bowels of the bureaucracy have not changed that.

I understand that you should go, and I suggest I'm trying to get rid of you before all these guys come back from the vote because if they do, you surely will be late.

Secretary KEMP. Well, thank you.

Senator BOSCHWITZ. We thank you.

Secretary KEMP. Thank you for your leadership. Thank you for what I consider to be a socially responsible market and free enterprise approach. I look forward to working with you. Thank you.

Senator BOSCHWITZ. Thank you very much, Mr. Secretary.

Would you just for the record introduce the two folks who are with you?

Secretary KEMP. Tom Humbert who is a deputy assistant secretary for policy development, and Mary Brunette, my special assistant for policy development and communications.

Senator BOSCHWITZ. We thank you again for being here.

We now ask the panel to come forward: Bob Woodson, Stuart Butler, and Dick Cowden. We are very pleased to have you gentlemen with us in the case of Mr. Woodson, once again. I get my Com-

mittees sometimes mixed up. I forget who testified at which Committee.

The order I see that has been designated here is Mr. Woodson, who is the president of the National Center for Neighborhood Enterprise, will proceed first, then Mr. Butler and then Mr. Cowden.

Do you have prepared testimony?

Mr. WOODSON. I have it here. It was not submitted.

Senator BOSCHWITZ. Do you have a prepared one?

Mr. WOODSON. No.

STATEMENT OF ROBERT WOODSON, PRESIDENT, NATIONAL CENTER FOR NEIGHBORHOOD ENTERPRISE, WASHINGTON, DC

Mr. WOODSON. The National Center for Neighborhood Enterprise is an organization that I founded 9 years ago to promote self-sufficiency and independence among low-income people around the Nation. And we have been cooperating throughout the years with Jack Kemp when he was a Congressman in promoting resident management ownership of low-income public housing throughout this Nation and worked with Members of the Congress on both sides, Congressman Dick Armey, Steve Bartlett, and Walter Fauntroy in passing some amendments to the Housing Act that would empower low-income people.

I would like to just comment on the importance of Enterprise Zones and economic incentives to address the more critical problems of low-income communities and low-income black communities in particular.

The problems that we have confronted and the program we have put in place over the past 25 years in waging the war on poverty have cost the Federal, State and local governments an excess of $1 trillion in programs to aid the poor. And although a third of the black community's condition is improving, one-third is in danger of becoming a permanent underclass. Proverty is clearly worsening in this group. Racial discrimination alone does not explain the conditions of poor blacks, as one-third of black two-parent households have incomes equal to 85 percent of white incomes, and the gap is closing at the rate of 5 percent per year.

We have found through our studies that the one condition that determines any ethnic group's participation in this economy is its small business formation rates. If you look at the various ethnic groups in this country to determine their participation in the American economy, you will find that blacks have about 6 percent of all businesses; Japanese Americans, by contrast, own about 30 percent.

Because 80 percent of all new jobs in the American economy are developed by small businesses, we, therefore, have to look at what the incentives are for promotion of strategies to promote business formation in low-income communities.

Ninety percent of the risk capital upon which small businesses depend comes from friends, relatives, and one's own savings. Most people do not have in those communities friends and relatives with that kind of disposable income.

Therefore, it is our firm belief that if we are to mount an effective war on poverty, it has to include Enterprise Zones that will

enable impoverished communities to stimulate small business development.

The National Center has been in the vanguard in identifying models of success where low-income people, once they are given the opportunity and the information, have, in fact, generated successful small businesses. One of these programs, recently highlighted on 60 Minutes, is in St. Louis, MO, the Cochran public housing project, in an area that was just devastated. In fact, the city wanted to blow the property up, businesses were fleeing, and development of new housing was virtually nonexistent.

But when the residents took over this development and began to manage it, screen residents and redefine themselves from victim to market, they began to improve the environment to the point where they were able to start small businesses; in fact, there has been such a dramatic turnaround in this community that for the first time in America in low-income public housing, there is market rate housing being built directly across the street from the development and is jointly developed with the public housing resident management company.

The residents living there are responsible for the development, share in this development because they are investors in the enterprise that they are moving in. They no longer call downtown, they are downtown.

And there are other examples around the Nation that we have chronicled and that we are bringing together.

And so, it is important for us to understand that in order for this revitalization of urban centers to continue to expand, we must have Enterprise Zones and a climate that will promote development of these communities.

And just one comment, Mr. Kerry and others, about affirmative action and set-aside programs. We do not believe that making a few blacks rich is economic development and that is what set-asides do. Affirmative action, programs should be based on income because it is the low-income black Americans who are not benefiting from affirmative action programs or set-asides. Set-aside programs benefit primarily middle income people who are developers.

I am not opposed to folks who are rich becoming richer, but I think we must be clear that this is not a strategy to address poverty. And, therefore, I think in our deliberations on Enterprise Zones we must look at real means and instruments to address poverty in America. I guess what I am pleading for is "truth in advertising."

In conclusion, Senators, we at the National Center continue to identify other examples of self-development in communities as a means to ridding our Nation of its current No. 1 scourge—drugs. On September 29, we are having a multi-city teleconference that will link 50 cities where grassroots organizations have effectively rid their community of drugs through various innovative strategies. It will be highlighted on a 5-hour teleconference emanating from the BIZNET studios where we will have an opportunity for the first time to go into these neighborhoods that have evidenced a willingness to develop themselves and see firsthand what is working and why.

And we think it would be very important for this kind of information to be shared with Members of the Congress because under-

pinning all of these efforts has to be economic revitalization if we are to provide an alternative to the drug trade.

We can't expect young people making $1,000 a week dealing drugs to accept a minimum wage job. Yet, how do we know whether or not these youngsters will choose the illegal economy—without a future—if we give them viable choices. Most of these youngsters know that they have never met a drug dealer who has retired. They know that the options that you face when you deal drugs are either the graveyard or jail, and those are heavy opportunity costs in any business, no matter how lucrative.

Many young people are dealing drugs only because we as a society have not provided them with viable alternatives. And that is why we are working every day to provide free market opportunities for young people in those communities to participate in legal means of doing business. And one of the strategies that will help create that environment is enterprise zones.

Thank you.

Senator LIEBERMAN. Thank you, Mr. Woodson. I am sorry I wasn't here when you began. Welcome to you and the other members of the panel.

Now, Mr. Butler, you obviously have been a real leader, as has The Heritage Foundation, in giving credibility and substance to the whole idea of Enterprise Zones, and we are delighted to have you here today.

STATEMENT OF STUART M. BUTLER, DIRECTOR, DOMESTIC POLICY STUDIES, THE HERITAGE FOUNDATION, WASHINGTON, DC

Mr. BUTLER. I appreciate very much the invitation to testify, Mr. Chairman, and also from you, Senator Boschwitz. In fact, it is not I believe the first time I testified before this Committee on Enterprise Zones. That was back several years ago in 1982 or 1983. And I think like many people——

Senator BOSCHWITZ. I remember you now that you started speaking.

Mr. BUTLER. You were, of course, with Senator Chafee, one of the leaders on the Senate side on the legislation.

And I think like a lot of people I threw away many of my files, thinking that the chance of a tax-based Enterprise Zone program had come and gone. What we are now seeing in the debate over this and in the discussions of real legislation to bring effective tax measures is in many ways the most amazing comeback since Lazarus returned from the dead. I think it is now about 10 years to the day since the first notions of Enterprise Zones were developed in this country, and it would be very fitting for legislation to be passed this year—to do what should have been done many, many years ago.

The debate that took place in the early 1980s over Enterprise Zones did lead to some very important results, even if it did not lead to legislation, particularly in the discussion of what it takes to get economic development occurring in very depressed areas, particularly in large cities. A number of very important conclusions came out of that debate which should be remembered by this Com-

mittee and by Congress as it looks to devise ways of applying tax incentives, necessary tax incentives, to put the State zones into overdrive. There are three particular things I would call to your attention.

The first is that when we are looking at Enterprise Zone legislation, we should be looking at a device to establish an atmosphere, a climate in the inner cities for creativity and for experimentation. We should not be trying to micro-manage economic development. Mr. Woodson and many others have demonstrated over the years the many very unusual and creative activities that nobody in this room, including myself—and including him probably—would have imagined could occur in the inner cities.

These are the kinds of things that we should be trying to encourage in the business area in the inner cities. So an Enterprise Zone Program, it seems to me, should not be trying to determine in advance what we shall be encouraging and what should we discourage. It should be trying to get that creativity out of the drug trade and out of the underground economy or just out of sitting around doing nothing and get it into action within the inner cities. So, I would urge you to look at a simple, fairly open kind of legislation rather than a very detailed program.

It is also very important to recognize—and we all do I think—the key importance of States and local governments in the process. There has been creativity among State zones—some good, some bad. All kinds of new ideas have developed at the State level. The Federal legislation should look at ways of encouraging that State creativity as a part of the overall strategy. That does mean retaining the idea of encouraging competition for designation among States and local governments.

Some people feel that it should be more or less an entitlement program, if you like, for cities. I very much oppose that. I think that the creativity that occurred certainly in the early 1980s among States, as they put their Enterprise Zone packages together, was in large part spurred by the thought that there was going to be competition for Federal designations at that time. And that encouraged creativity, as all competition does. So, I would strongly urge that any legislation does retain that notion of a competition for designation.

I would say thirdly—and it is most appropriate in front of this Committee—that we must always see the primary business activity that we are looking to encourage in Enterprise Zones as small business activity. The Enterprise Zone legislation should not be a device to try and lure large corporations back into the inner cities. It should not be a massive tax giveaway to large corporations. Many States currently and wrongly have used that latter approach, and I think it is a profoundly wrong way to try and deal with the problems of the inner cities.

There are many reasons for basing an Enterprise Zone Program on small businesses. We know that that is where the jobs come from. They are the primary generators. As Mr. Woodson has said, if we are talking about creating businesses in the minority community and in the poor community, we are not talking about creating Fortune 500 companies. We are talking about establishing small businesses that can grow over many years.

We should also be very aware of the location decisions that are made by companies. When you review the literature and the decisions that are made as to why companies locate in particular places, for large corporations we find that the tax incentives tend to be very low down the list. Issues like a skilled workforce, and so on, are far more important. If you are trying to use taxes to lure a large company into a very depressed area, they have to be massive tax benefits—as cities are discovering.

So, I think that there are many, many reasons to lead this Committee and Congress to the conclusion that an Enterprise Zone Program should be based on small enterprises.

That, of course, leads you then to consider what kinds of tax incentives are appropriate to small enterprises and to new enterprises that are likely to be the kinds of firms interested in a South Bronx or an inner city Detroit.

I have talked to lots of small business people and to organizations representing them about this particular issue, and they tell me a number of very specific things. They say that first of all any tax incentive for a new small business run particularly by a first-time businessman has got to be simple. When small firms start up they don't tend to have a cadre of tax attorneys behind them interpreting regulations and requirements. So, keep it simple.

They also say that if you really want to get small new businesses off the ground you have to focus on things that encourage capital to flow into those businesses and also deals with their cash-flow, the payroll and basic costs that they face in the immediate term.

If you recognize that and look at an Enterprise Zone legislation that would help with that, some very specific things flow out. Many are contained certainly in the legislation that you have put forward. The idea of an immediate writeoff for the purchase of stock within an Enterprise Zone company provides an up-front, immediate incentive to take the risk of going into that area. I think that is a very important device and should be retained.

The emphasis on capital gains tax relief is extremely important because that is a reward to risk, and we are talking about high risk. Therefore reducing or eliminating the capital gains tax is agreed by the individuals I referred to as a very important stimulus to get people to risk their money in these areas.

I think one thing you might consider adding to the legislation would be not only the freedom of capital gains for rollover of investments moved around in an Enterprise Zone or between Enterprise Zones, but maybe a onetime or lifetime tax exclusion against Enterprise Zone profit, much like you have in the real estate market where if you are over 55, you can take a onetime exclusion. Let us reward the people who put their lives into businesses over the long haul in an Enterprise Zone, give them the kinds of tax breaks we give to middle-income people who invest in real estate.

I would also say that it seems to me that an emphasis on capital gains tax relief would be more effective if one had to make a choice than, say, an investment tax credit or any tax exempt instruments to encourage the flow of capital into those areas. I think a clean, simple capital gains tax reduction or elimination would be the preferable approach.

If one was to try and limit the potential tax loss through a capital gains relief—and I share the view of Senator Kasten and Secretary Kemp about that, but for the sake of argument, assuming that there is a loss—perhaps again one can look at the idea of a limit on the total amount of money that can be put into a small business in an Enterprise Zone and gain that exemption from capital gains. That would make no difference to a small enterprise, but might avoid people using Enterprise Zones as a sort of tax haven rather than as a way of generating new jobs and employment within those areas.

In the second area I mentioned, that of labor costs, the legislation does have a nonrefundable tax credit for employment of disadvantaged individuals within those areas. I think that is very important and useful. Of course, a nonrefundable credit does mean that if a business is starting up and not making profits and not paying taxes on profits, that credit is not so effective to them.

I do understand why there is resistance to making that a refundable credit, but you might consider looking at introducing an earned income tax credit element into the Enterprise Zone legislation which is refundable. It is already on the books, and would be a way of giving an incentive indirectly to the employer by allowing the take-home pay of an employee to be increased by virtue of being in an Enterprise Zone. There are ways of improving at the margin that incentive that is currently in the legislation.

Let me just say once again in conclusion, Mr. Chairman and Senators, it is 10 years since we began to look seriously at Enterprise Zone legislation. It has been a long road. We had legislation passed in 1987, which, as Secretary Kemp said, was a very modest step—very, very modest—that really needs to be enhanced. We also have State zones. What we need now is that final instrument of effective and powerful tax incentives at the Federal level to enable Enterprise Zones to be a real potent device.

Senator Lieberman, Secretary Kemp mentioned your mutual interest in Winston Churchill, so may end with a quote from Winston Churchill regarding the tax incentives that we must have, "just give us the tools and we will finish the job" on Enterprise Zones.

Thank you.

[The prepared statement of Mr. Butler follows:]

HOW TO DESIGN EFFECTIVE ENTERPRISE ZONES LEGISLATION

Testimony before the
United States Senate
Committee on Small Business

21 September 1989

Stuart M Butler
Director, Domestic Policy Studies
The Heritage Foundation
Washington, D.C.

My name is Stuart Butler. I am Director of Domestic Policy Studies at The Heritage Foundation and I have been studying the theory and practice of enterprise zones for the last ten years. I would emphasize that the views expressed in this testimony are my own, and should not be construed as an official position of The Heritage Foundation.

It is heartening to see Congress apparently moving to take action on the enterprise zone idea, some ten years after the concept was introduced from Britain. Senator Boschwitz is to be commended for once again being in the lead in pressing for legislation, just as he was in the early 1980's. Similarly, it is good to see Jack Kemp, this time as HUD Secretary, also leading the campaign as he did when the idea was first introduced.

While the early debate over enterprise zones did not lead to any federal legislation till 1987, when a very diluted form of the idea was enacted, that debate did have two very important results. First, it sparked an intense discussion over the nature of economic development in depressed neighborhoods. This discussion led to a much better understanding of the importance of small firms in job creation, and also the vital importance of community-based organizations in mobilizing local resources and

talent. We now understand that if there is to be strong economic development in the inner cities, the core of business activity must come from small enterprises.

The second result of the debate in the early 1980's has been the passage in over 30 states of state-based enterprise zones. These state zones, beginning with Connecticut in 1982, have brought heartening results despite the weak tax incentives available at the state level. The study of the New Jersey Enterprise Zone Program, the most recent analysis of a state, corroborates the general finding that well-designed state enterprise zones can have a significant impact on economic conditions in depressed areas. This body of experience at the state level bolsters the argument that a federal enterprise zone program, with its more powerful tax incentives, could have a decisivm effect on the economy of America's inner cities.

With the enterprise zone legislation introduced in the House earlier this year (HR6) by Congressman Rangel, and the similar legislation introduced in the Senate by Senator Boschwitz, we have an opportunity to enact strong and effective enterprise zone legislation to help revive the inner cities. But if the support for enterprise zones among both congressional leaders and the Bush Administration is to lead to effective legislation, Congress must remember the debate of the 1980's and design legislation founded on the fundamentals of urban development

crystallized in that debate. This suggests that Congress should craft new legislation based upon several key principles:

1) Enterprise zones should spur creativeness, not attempt to micromanage economic development.

The enterprise zone concept is based on the notion that even within very depressed areas there are resources -- often dormant -- that can become the basis of new economic activity. Even in such blighted areas as the South Bronx there are underused or vacant buildings that could become the home of small firms. There are aggressive and creative community organizations that can mobilize the people to tackle the social problems that discourage enterprise. And there are in fact many small enterprises either operating in the underground economy or engaged in illegal activity. By reducing the barriers to legitimate enterprise, these resources can be brought together in economic development for the benefit of the entire community.

In order to ignite economic activity, the enterprise zone programs should focus on establishing the best economic climate to foster entrepreneurship. But the proposers of the concept do not, if there are honest promoters, argue that it is a panacea. Other ingredients are required for economic development, many of which are not strictly economic tools. Action needs to be taken, for instance, to tackle the staggering progress of drug use and

crime within the inner cities: the National Drug Policy recently unveiled by the Bush Administration has a key role in tackling this deterrent to legitimate enterprise. Similarly the problems of the schools must be addressed, by introducing strong parental involvement through such devices as open enrollment and site-based management of schools. In addition, a policy for the inner cities must allow community-based organizations to take a leading role in providing services within the neighborhood. That is why Secretary Kemp's strong support for resident management of public housing is so important. Similarly heavy welfare dependence in the inner cities must be reduced through innovative welfare reform initiatives, such as those spearheaded in recent years by the states and made possible through waivers from federal regulations granted by the Reagan Administration.

Thus enterprise zones should be seen as an economic dimension to a general strategy of stimulating creative and empowerment in the inner cities. Enterprise zones are one vital ingredient in what should be seen as a new war on poverty, where blighted urban neighborhoods is the first battlefield.

This emphasis on encouraging creativity by the "local troops" in the war suggests that federal policy in general, and a federal enterprise zone program in particular, should not try to micromanage initiatives in each neighborhood. Conditions are very different in different places. An approach that works well

in one city may be ineffective in another. Thus we need to guarantee the highest degree of freedom for cities and their neighborhoods to experiment with new ideas to promote economic activity. Much like the frontier during the great movement west in America, where the remoteness of central government allowed creative local solutions to be applied to problems and opportunities faced by pioneers, so the inner city should be seen as an "urban frontier".

Thus an enterprise zone strategy should confine itself to establishing the best possible climate in incentives and barrier removal, and then allow those closest to the situation to design the details of the strategy. This means Congress should not load up an enterprise zone program with a wide range of well-meaning financial packages or finely-tuned incentives designed to promote particular kinds of ventures. It would be far better to establish broad powerful stimulants to economic activity within a relatively simple framework, and allow a thousand flowers to bloom.

2) Assure Competition in the Designation Process

There are some supporters of the enterprise zone idea who argue that federal enterprise zone incentives should be applied to any area that meets certain eligibility requirements. Such an "entitlement" approach would be a mistake. Enterprise zones

should not be seen as federal manna from heaven, descending upon cities, but rather a federal dimension to complement a process of creative economic policy at the state and local levels. When it seemed probable in the early 1980's that Congress would pass legislation to establish a limited number of zones, states and cities began devising very innovative strategies for economic development. Their aim was to have an "inside track" in the selection process for designation, should a federal program be enacted. Had Congress been considering an entitlement program for enterprise zones, there would have been no such stimulus for this creativity.

Thus I would urge Congress to stay with the principle that enterprise zone legislation should be seen as limited in its extent and in the number of designations, in order to encourage new approaches at the state and local level.

3) The Importance of Small Business

Many state and local development officials continue to believe that the best way to assure economic growth in a poor neighborhood is to encourage large companies to locate there. The assumption is that a firm employing, say, 100 people, must be better than one employing 3, and that large firms become the nucleus or anchor for economic expansion.

In almost every instance this is an unwise strategy. The fact is that large firms are poor generators of new jobs. Research by David Birch at MIT and others indicates strongly that it is small firms that are the primary generators of jobs in the U.S. -- the large firms in recent years have shown a net loss of net new jobs. But large companies are not appropriate targets for another reason. Studies of location decisions of large firms indicate that chief among the factors influencing the decision are the availability of properly trained employees and an environment conducive to attracting skilled workers and managers. Tax incentives are well down the list of factors. Thus when a city attempts to retain a large company, or attract a new venture to a blighted neighborhood, through a package of tax and other financial incentives, that city tends to find the price is extremely high. This price is increased by the understandable reluctance of other cities to accept the relocation of one of their large firms. Thus we tend to see a "war of incentives" between competing cities with a very high price for the taxpayer and often very little real economic stimulus to the city that "wins" the competition.

Thus an enterprise zone program would be both expensive and largely inefficient if it sought to recruit large companies to depressed urban neighborhoods. Instead the focus should be on creating the conditions necessary to generate new small enterprises, preferably drawn from the resources within the

neighborhood itself.

Other than the practical reasons of job generation and location decisions, there are many other reasons for focusing on small enterprises as the foundation for economic recovery in depressed areas. For one thing, small firms tend to be more creative, can be most innovative and adapt to unusual economic and social conditions. The urban analyst, Jane Jacobs, in her book, The Death and Life of Great American Cities, points out that risk-taking, innovative firms need to keep overhead costs as low as possible, so they tend to locate in older buildings and neighborhoods where costs are low. Firms based on tried and trusted ideas locate in new buildings and neighborhoods. In addition, small firms require modest capital and usually less sophisticated technology and management skills. Clearly these firms are more appropriate for areas where capital and skills are in short supply.

Small firms, moreover, can be established by city-based organizations as part of their general program of reviving a neighborhood. One of the interesting features of the growth of tenant management in public housing, for instance, is that these management associations very quickly diversify into and create businesses to both employ local residents and to improve the availability of goods and services to the neighborhood. In this way, the economic objectives of the enterprise zone strategy can

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be combined with a more general approach to addressing the conditions of an inner city.

4)Tax Incentives Should Stimulate Small, Start-up Businesses

This focus on new, small business creation as the foundation of an enterprise zone strategy suggests different tax incentives than we would use in a program aimed at larger firms. It also means that any enterprise zone program should also aim at the costly burden associated with local regulation. If we are to foster the growth of small enterprises within large dilapidated resident neighborhoods, the program should encourage local authorities to streamline zoning, building codes and other regulations and permits that can be an enormous obstacle to a small firm. Even simplifying the regulation process in the form of "one-stop shopping" procedures can be enormously beneficial by reducing the delay and thus cost of waiting for appropriate permission.

In the case of tax incentives, the proprietors of small firms correctly point out that they lack the sophistication to use complex tax incentives. Thus, simple tax incentives are required. They also emphasize that their primary need is not reduction of taxes on profits -- most make little or no profit in their early years on which to pay taxes -- but tax measures that will encourage investors and lenders to provide them with

the working capital and the long-term capital they need to develop their businesses. In addition, small firms, particularly those in high-risk depressed areas, tend to be chronically short of cash. Thus incentives that improve their cash flow, enabling them to take on labor and meet the other routine requirements of running a business, can be extremely helpful in assuring success.

This suggests that Congress should focus on two broad forms of tax incentive in a federal enterprise program:

A) Taxes on Debt and Equity Capital. In order to provide an incentive for lenders and investors, Congress should consider the elimination of capital gains taxes for investments in enterprise zones. This would encourage investors to take the higher risk of putting their money in a depressed neighborhood, and it would encourage the proprietors of enterprise zone businesses to build them up over the long haul.

Such relief from capital gains taxes should not be restricted to certain types of investment. Restricting the relief, say, to investments in new structures or physical redevelopment would shift economic activity away from less capital-intensive ventures that may in fact be more appropriate to the neighborhood.

Concerns about the potential cost of such tax relief can be

addressed in several ways. My suggestion is that the tax incentives be structured much like the capital gains tax relief on the purchase of a home. In the case of housing, the gain is not taxed until it is eventually taken out of housing rather than simply being rolled over. In addition, there is a one-time exclusion for those over the age of 55. A similar approach could be used in an enterprise zone. If an individual rolls over a capital gain in an enterprise zone business into another enterprise zone venture, the gain would remain free of tax. Only when the net gain was taken out of the zone would tax apply. In addition, an additional benefit to encourage smaller investors would be a one-time capital gain exclusion of, say, $100,000.

This limit on the total exclusion of a capital gain would discourage investors and businesses from using enterprise zones as tax havens (while providing little economic stimulus to the neighborhood -- yet be a powerful inducement to small business. Another way of limiting the cost of the total package -- while retaining the powerful stimulus to small enterprise -- would be to place annual limits on the amount of an investment by an individual taxpayer that would be subject to any tax benefit. In addition, the amount of investment funds received or money borrowed by a firm that provided tax relief to the investor/donor could be subject to an annual limit. In this way, the full tax relief would apply to small firms, but a large firm would find the available tax benefits to be small in comparison with its

scale of operations. As mentioned earlier, tax relief is in any case a marginal consideration in location decisions by large firms, and so these limits would be an effective safeguard against the potential for run away costs and for the enterprise zones to lead to major firms using them as a tax loophole without having much local economic impact.

B) Payroll Taxes. Payroll costs are the other major obstacle for small firms in depressed neighborhoods, and so the program should address this issue. The legislation now before Congress addresses this by applying non-refundable income tax credits for certain types of employees. I suspect this may be the wrong mechanism. Making the employment credit non-refundable certainly would reduce the cost of the program and avoid breeching the principle of not providing cash benefits to employers. But it would mean that small start-up businesses, typically not paying taxes on profits, would have little benefit from the credit.

Perhaps a better strategy would be to provide tax relief to the employee instead, by using enterprise zones as a demonstration area for an Enhanced Earned Income Tax Credit. The current credit would be both increased and linked to the size of the family. This would allow take-home pay for lower-paid workers, particularly those leaving welfare or with large families. The employer would not need to be sufficiently

profitable to use a non-refundable tax break. Designing the employment tax relief in an enterprise zone, as a form of an expanded EITC, probably would be more effective than the current legislation's combination of non-refundable credits for both employer and employee.

This renewed interest in passing tax-based enterprise zone legislation is an important step forward in addressing the problems of depressed neighborhoods. The conditions in many areas may be far worse than when the concept was first proposed in the U.S., but there are also grounds to believe the concept might yield better results today. We have learned a great deal in the last ten years about the nature of the problem and the potential for various approaches. Pouring money into the inner cities has not succeeded in the past and there is little evidence to suggest it will do so in the future. Instead we should launch a strategy based on stimulating the dormant entrepreneurship within depressed areas themselves, combined with steps to empower residents to exercise greater control over their housing and education. Such an approach would be based on the knowledge we have acquired in recent years that improvement in a poor neighborhood can occur only if it is led from within.

Senator LIEBERMAN. Thank you, Mr. Butler. A perfect way to conclude.

We had the pleasure of the company for a brief period of the real Chairman of this Committee, Senator Dale Bumpers of Arkansas. I appreciate his authorization to——

Senator BOSCHWITZ. You have been misleading me? [Laughter.]

Senator LIEBERMAN. Well, I am just acting for the day.

He leaves a statement for the record, and Senator Boschwitz and I thank him for authorizing us and encouraging us to go forward with this set of hearings on Enterprise Zones.

[The prepared statements of Senator Bumpers and Baucus follow:]

Statement of Senator Dale Bumpers

I am pleased to welcome Secretary Kemp to the Committee on Small Business and look forward to hearing his views on the subject of enterprise zones. Jack Kemp is to be commended for his steadfastness in advocating this idea, even in the face of opposition within his own Administration.

In my view, it is unfortunate that this issue has, in the past, become entangled in partisan Congressional politics. As Congresswoman Oakar told the Committee in our previous hearing on this subject, there have been Democrats and Republicans in the House, particularly including Congressman Rangel, who have championed enterprise zones for many years.

What is clear to me is that we have a desperate need in many parts of this country for bold economic development programs. The HUD Secretary has naturally focused most of the frightening problems facing many of our larger cities. I simply want to remind him that the fierce problems of drugs and lack of housing and jobs are equally real for millions of Americans who live far from the bright lights.

For two years or more, I have been trying to call attention to the deplorable economic and living conditions in the Mississippi Delta. Taken as a whole, many of the counties in

Eastern Arkansas, Western Mississippi and Northeastern Louisiana lag behind many of the Third World countries to whom we send foreign aid. No doubt, the same can be said of dozens of blighted urban areas in our Nation's inner cities. Jack Kemp has forthrightly called attention to these long-suffering areas in the cities. At least the current Administration has been more realistic than the previous one in recognizing the face of human suffering.

Enterprise zones continue to be the topic of heated debate among learned economists. The case can be made that this program only shifts economic growth from one area to another, rather than increasing the total economic pie. However, on behalf of the "have nots", we are not all that concerned where the growth comes from at this point. Clearly, and largely due to federal policies such as huge and unbalanced military spending, some parts of this country have lived high on the hog for the last ten years or so, while others have gone begging. As the old saying goes, it's time to do something even if it's wrong.

I am open-minded about enterprise zones and would seriously consider any program which provided adequate opportunities for economic improvement in rural America. I look forward to the testimony of Secretary Kemp and today's other witnesses.

Statement by Senator Max Baucus
for the Senate Small Business Committee
Hearing on Enterprise Zones
September 21, 1989

Mr. Chairman, I would like to thank you for holding this hearing today.

I think enterprise zones can be an important tool in fostering business development in economically distressed areas.

The Senate Finance Committee has held several hearings over the past couple of Congresses to take a look including tax incentives in any federal enterprise zone package.

Several enterprise zone bills with tax incentives have been introduced this Congress in both the House and the Senate.

As many of you know, one of my priorities this Congress is to help provide rural areas with the tools necessary to foster business investment.

To that end, I have introduced four bills to

help equalize some of the disparities between rural and urban America.

One brings state-of-the-art telecommunciations services to rrual areas so that they can join in the "Information Age" of the future.

The second sets up a public/private partnership mechanism to bring more high risk capital to rural areas for business investment.

The third will better enable rural communities to establish business incubators for the purpose of lowering overhead costs.

And the fourth will make the Essential Air Service program and entitlement to be paid for out of the Airport and Airway Trust Fund.

The first three of these bills have been included in S. 1036, the Rural Partnerships Act of 1989, which passed the Senate on August 2. And the fourth I hope to have included in the budget reconciliation bill.

I am currently working on developing an enterprise zone package for rural areas which will

include various tax incentives.

That is why I am very interested in the subject of this hearing today and thank the chairman for holding it.

Senator LIEBERMAN. Mr. Cowden, executive director of the American Association of Enterprise Zones, we look forward to your testimony now.

STATEMENT OF RICHARD COWDEN, EXECUTIVE DIRECTOR, AMERICAN ASSOCIATION OF ENTERPRISE ZONES, WASHINGTON, DC

Mr. COWDEN. Senator Lieberman, Senator Boschwitz, the American Association of Enterprise Zones represents literally scores of cities and States around the country who are using the Enterprise Zone Program as part of their redevelopment policies. And it is interesting to note that we are probably as diverse and as pluralistic a group as the Congress itself. And yet, there seems to have been much less of a problem among our members in those cities and States in reaching the necessary compromises to implement effective Enterprise Zone Programs than there has been here in Congress. For some reason, Congress has not been able to put together a formula that is necessary to get a Federal Enterprise Zone Program in place.

Perhaps we would suggest that by studying what the cities and States are doing, we can serve in effect as a laboratory both in an administrative sense—just what is working out there and what is not—and also in a political sense—compromises between goals among competing groups that want to see their views prevail. How do you get all those groups represented in an Enterprise Zone Program? I think we serve as a good example of how that gets done.

Over the years we have talked to hundreds of cities about what they are doing. And we know, just from the seat of our pants, what is going on there, and we do see examples of success. We have been reporting those successes. But until recently, unfortunately, there really has not been much more than anecdotal academic research in this field.

Even a recent 1988 GAO report sought to draw general conclusions about the city, State and, in fact, the Federal program from examining only three State programs in Maryland, none of those including anything but tax incentives. Anyone who knows anything about Enterprise Zones in this day and age realizes that they include in the best cases much more than just tax incentives.

It is fortunate that recently we have had a group of Penn State researchers who have been analyzing some HUD data and have come up with significant results from over 300 cities in 17 States. They found that the average zone was gaining over 460 jobs in a fairly limited time. In fact, they found that a quarter of the zones studied were showing better performance than average urban areas around the country. As you know, zones are manifestly distressed areas, and yet many seem to be performing even better than average areas.

A report on the New Jersey Enterprise Zone system that was released just this summer has reported that there were over a thousand businesses creating over 9,000 jobs and adding $243 million to the payroll in those areas. The New Jersey report confirmed what reports in Indiana and California are coming up with now—that Enterprise Zones are performing an important catalytic role in

bringing together redevelopment programs that involve both tax incentives and other kinds of improvements.

These reports are really confirming what our members have been saying for years, which is that Enterprise Zones are not a miracle cure, but are an effective way of focusing whatever redevelopment resources are out there and available.

We have found that the best zones are those that incorporate not just tax incentives, but also direct redevelopment assistance—improvements in the actual physical infrastructures of the cities, and improvements to the services that are available to the businesses and the residents of the zones.

Our research has also confirmed what a HUD study has found, which is that Enterprise Zones send a positive message to the business community. They are the sign of the city and State that they want these areas to improve. And there is a kind of logrolling effect, where property values and business opportunities seem to improve just because the city and State say that they expect them to.

In 1987 Congress approved the Housing and Community Development Act, which included title VII, authorizing 100 Enterprise Zone designations. That began to make our people hopeful that there would be an effective zone program coming down the road. But, unfortunately, it did not include tax incentives. And Secretary Kemp has said, at least for the time being, that he does not want to designate those zones at least until they include tax incentives.

We appreciate this point of view, and we hope that Congress can help him and us finish the work that we have come so close to completing by enacting a thorough-going Enterprise Zone Program.

We have a few general suggestions and a few specific suggestions on how the Committee and the Congress should approach the Enterprise Zone Program.

First we think that the most important role of the Federal Enterprise Zone Program is not incorporated in the specific incentives themselves—which tax incentive is best; whether a tax incentive is better than another kind of incentive—but how effectively the program is used as a carrot to prompt more activity by the cities and States.

I want to echo what my friend Stuart has said. In fact, he sort of stole my lines here because we have been campaigning for a competitive designation system for a long time. And we think that the program will not work unless the designation system both is based on distress standards and compels the cities and States to do more than they are doing now to make improvements in those areas.

In fact, when we surveyed our own people recently, we found that Governors and Mayors would be willing to devote more of their resources to making improvements in the zones if they thought that would increase their opportunities to participate in a Federal program. And I think that suggests the need for a competitive element.

The second general piece of advice that we have is not to consider Enterprise Zones—the Federal program—as a stand-alone program, but to see it in light of what the cities and States have been doing already. I think a lot of us, even among our allies, tend to think, well, what will this Federal incentive or this Federal pro-

gram do? And then they start to do a cost/benefit analysis of what a particular incentive is going to do. They do not see it in terms of being linked to the ongoing work of the cities and States. And further, they tend not to look into what synergies might be produced by that kind of linkage.

And finally, even though we have been throwing out statistics ourselves, we would encourage you not to be preoccupied with statistical assessments of Enterprise Zones. There has been this tendency for us to say Enterprise Zones will create X number of jobs. Then the opponents always say those jobs would have been created somewhere else anyway. So, they count every dollar of incentives as being a total loss to the Treasury.

We find that to be a completely cynical point of view of urban policymaking because the location of jobs within an urban area is a critical consideration. In fact, as you well know, Federal policymaking does affect those decisions. We note the beltways and the interstate highways that have effectively drained the inner cities in many ways of economic vitality. And, therefore, we do not think it is outrageous to expect that a certain limited amount of Federal resources should be devoted to encouraging reinvestment in the inner cities and distressed rural areas.

A couple of specific recommendations that we would like to look at are: A targeting feature should be involved in any Federal Enterprise Zone Program. This can be done without new appropriations. It does not mean that Enterprise Zones must become a spending program. This could be done through both administrative decisions, possibly an Executive order or some kind of an executive policy by the Administration. It could be sustained and encouraged by legislative language.

In fact, the title VII provisions did include something of this nature that we think should not be underestimated. A lot of zones believe areas that are designated as Enterprise Zones, where States are devoting an extra measure of their effort, should get priority in receiving Transportation funds, Labor funds, HUD, SBA, EDA. Any agency that deals with economic development should have some policy on Enterprise Zones that gives priority to those areas.

Another feature that should be looked at is the need to emphasize job training. A lot of the zones were suffering from shifts in technology, plant closings, and so forth. And even possibly through the mechanism that is provided by the Job Training Partnership Act. Perhaps we can make job training funds more available in the Enterprise Zones.

Another of the suggestions of our members is an investment credit that would promote the retooling of a lot of older plants in these older areas. That incentive is lacking from even the Administration's program, which does include a capital gains feature. But that does not affect machinery and equipment. It affects only the buildings themselves. We think there needs to be some incentive to reinvest in machinery.

Finally—this falls along the line of a new idea—we have been asked to look at the standing foreign trade zone feature in the Enterprise Zone bill and to look at how this could be improved. This is, frankly, along the lines of a Hail Mary pass, but I think that it would have a profound effect if we could essentially treat these

areas as if they were developing countries in terms of a free trade zone designation. In other words, any manufacture of items that includes foreign components and involves a threshold level of value added in the zones could be entered into the country duty free. This is pretty much along the lines of the Generalized System of Preferences, which requires 35 percent minimum value added in a developing country in order to have duty free access to the United States.

We have recommended this both for Enterprise Zones and for any Indian reservation. This is kind of a revolutionary idea. We would like to see what would happen if an experiment of this nature were held out as part of our trade policy to encourage our trading partners to allow our companies to invest in their low income areas and enter products on a duty free basis into their countries.

In conclusion, I would just like to add that Enterprise Zones have become a routine and a well-accepted redevelopment tool around the country. There is very little controversy about Enterprise Zones in most places where they are being implemented. And in the best of all cases, Enterprise Zones could become a common and linked strategy to bring in all levels of community interest in redevelopment together for the betterment of those neighborhoods.

The States have already deployed a very effective and useful framework for this kind of approach, and what they need right now is reinforcement from the Federal Government in order to make their programs come alive.

Thank you.

[The prepared statement of Mr. Cowden follows:]

TESTIMONY PRESENTED

TO THE

SENATE SMALL BUSINESS COMMITTEE

BY THE

AMERICAN ASSOCIATION OF ENTERPRISE ZONES

SEPT. 21, 1989

Our organization represents the many scores of cities around the nation that have adopted enterprise zones as an element of their urban redevelopment strategies. Our members operate zones in the inner cities of large metropolitan areas, as well as in isolated rural areas and on Indian reservations.

The Association is as pluralistic as the country itself and the makeup of our membership reflects the diversity that we find in the House of Representatives and the Senate. As many on the committee are aware, the federal enterprise zone proposal has been before Congress for almost the entire decade of the 1980s. But as yet no political formula has been developed to produce a federal zone law.

Even in the absence of such a policy, the cities and states have used enterprise zone techniques effectively.

Rather than causing political divisiveness in the states where they have been implemented, the zones have tended to bring communities together. The wide acceptance of zones in 37 states has been made possible by the willingness of state legislatures and local governments to reach compromises in order to carve out a workable redevelopment program.

Not only do our members' experiences highlight the need for Congress to adopt a similar bipartisan approach to urban policy making, they provide a wealth of information about effective zone techniques. In short, we offer Congress a political and an administrative laboratory for the issue that is before you now.

For many years our organization has reported examples of successes in enterprise zones. Until recently, however, little academic research has comprehensively examined enterprise zones. Even a 1988 Government Accounting Office report that has received an inordinate amount of media coverage drew general conclusions based on only three enterprise zones in the State of Maryland.

Fortunately, in recent months more exhaustive studies conducted on the basis of statewide and nationwide data have yielded more statistically significant information on zones. In June of this year a Pennsylvania State University team who examined data from over 300 zones in 17 states found that new investment in the zones resulted in an average gain of 460 jobs. About a quarter of the zones studied performed better

than the national average for urban areas during the period studied. The team noted that this finding was especially significant in light of the fact that the zones were areas of economic distress.

A study of the New Jersey program released this summer identified about 1,000 firms locating in the state's 10 enterprise zones between 1985 and 1988. These new businesses generated over 9,000 jobs and accounted for $243 million in payroll. This report, like those conducted during the past two years in Indiana and in California, gave the zones generally good marks both in overall performance and in cost/benefit ratios. The state-level researchers also echoed the Penn State team's conclusion that the zones have played a "catalytic role" in promoting redevelopment of decaying neighborhoods.

These studies confirm what our group has learned over the years. Since we first began working with state and local administrators, they have been telling us that zones are not a miracle cure but a useful means of focusing redevelopment assistance in distressed areas. We have discovered that zone programs incorporating a wide variety of incentives, as well as physical and service improvements, usually are found in communities with the most thoroughgoing commitment to redevelopment. And those zones are predictably the ones that perform best.

Our feedback from the cities has also confirmed a U.S.

Department of Housing and Urban Development finding that the state designation of a neighborhood in and of itself sends a positive message to the business community. Thus, zones are a sign of city and state interest in revitalization.

The 1987 passage of the Housing and Community Development Act, contains authority to designate up to 100 zones, albeit without federal tax incentives. With the adoption of that proposal, our members became hopeful that the federal government would at last add its support to and express its interest in a redevelopment strategy coordinated with the existing zones. We fully appreciate Secretary Jack Kemp's reluctance to proceed with the designations until Congress authorizes a complete incentive package. In doing so he has thrown down a gauntlet to Congress. In effect, he has challenged the House and Senate to make enterprise zones more than a symbolic commitment.

Speaking on behalf of our members, we urge the Committee to take Mr. Kemp's gesture to heart and help us finish the useful work that the cities and states have begun with regard to enterprise zones. At the same time, we are concerned that Congress not miss the opportunities presented by both Title VII and the enterprise zone proposals that have been introduced this year.

The American Association of Enterprise Zones can offer some general suggestions on how to approach its work on enterprise zone legislation. First, the most important role

of a federal enterprise zone policy is to serve as a carrot for the cities and states themselves. Regardless of what incentives are included in the law that eventually wins approval, any selection process should be established on a competitive basis, rather than strictly on a rank order of distress criteria.

A recent survey of our own members indicates that mayors and governors would be willing to direct more resources to the zones if they believed their public investment would enhance the chances of inclusion in a zone program that involved federal participation. This suggests that the designation process should favor localities making real, verifiable commitments to offering business incentives, as well as improvements to infrastructure in the zones. If implemented in this manner, the federal enterprise zone program can have a double impact; it will appeal to private sector investment, while prompting the cities and states to concentrate their redevelopment efforts in areas of greatest need.

Second, the federal program should not be regarded as a stand-alone policy, but should build upon the work that the states have begun. This means that Washington should not look upon designation of 50 or 100 zones as the ultimate goal. Rather, the federal government should develop ways to shape the actions of the many hundreds of communities that operate zone programs and it should formulate a systematic

means of tracking their performance as a guide to future federal urban policy.

Finally, we would urge the Committee not to become preoccupied with statistics as you evaluate what actions to take in regard to enterprise zones. For example, critics often charge that every job created in the zones would have been created elsewhere. They then conclude that any cost attributable to the program amounts to a total loss of government resources. This logic is one of the primary reasons why a zone bill has not passed already.

Our organization regards this as a cynical view of federal urban redevelopment policy. The location of new businesses and employment is a crucial public policy issue because of the restricted mobility of many residents of low-income neighborhoods. Affluent suburban communities have all the advantages in attracting new businesses. And much of that is due to federal decisions, such as expenditures on modern interstate highways and beltways that have contributed to the drain of investment from the inner cities.

Devoting a limited level of federal resources to encourage reinvestment in distressed areas should not be as controversial as it has become. At the very least, revenue reductions assigned to an enterprise zone policy should be balanced against some estimate of the value of bringing employment opportunities closer to people who would otherwise remain dependent upon federal transfer payments.

We can also suggest the following specific provisions that may merit consideration as the Committee evaluates possible features of a new enterprise zone initiative:

- Targeting of existing economic development programs. Even without new appropriations, Congress and the Administration can help the states improve the services and infrastructure in enterprise zones by adopting a policy that targets the designated areas. Enterprise zones should receive priority in the allocation of assistance through all federal agencies that have an economic development function.

- Incentives for job training. Many of the zones experience acute unemployment problems due to individual plant closings and shifts in technology. The federal enterprise zone policy should emphasize training and retraining assistance, possibly through the mechanism provided by the Job Training Partnership Act.

- Investment incentives. The program should include a tax credit for companies that invest in new plant and equipment in enterprise zone-based operations. This provision is vital to stimulating the

retooling of many aging facilities in older industrial areas.

- Duty-free treatment for items manufactured in zones. The leading federal enterprise zone proposals have long included a provision that would give priority to designation of foreign-trade zones. Congress could significantly strengthen this provision by experimenting with an incentive that would amount to the establishment of a true "free trade zone" program. We recommend that Congress evaluate the benefits of allowing duty-free treatment for the manufacture of items containing foreign components but a threshold level of value added in an enterprise zone.

  The 35 percent minimum value added standard that applies to developing countries under the Generalized System of Preferences could serve as a guideline for this provision. Not only would such an incentive serve to attract investment and employment in the zones, it could become a valuable demonstration of free trade principles for American trading partners that wish to attract our investment.

In conclusion, we should note that enterprise zones have become a well accepted and routine part of almost every state's economic development program. The enterprise zone concept could offer all levels of community interest in America a common and linked strategy for addressing urban redevelopment issues. The states have already deployed a widespread and remarkably useful framework for this process. What we need now is a federal component that reinforces local initiative.

I appreciate the opportunity to speak on behalf of the American Association of Enterprise Zones. Our members and I will be happy to respond to any questions you may have about our work with this unique redevelopment tool.

Senator LIEBERMAN. Thank you. That was very helpful testimony. I don't think Doug Flutie could have thrown a better Hail Mary than that last one. That was a good one.

All of you have been very good witnesses and we appreciate your presence.

Let me just pick up at the end with something you said that is implied in the testimony of Mr. Woodson and Mr. Butler as well.

Is there now any controversy about whether the Enterprise Zone idea works or whether it is worth the lost revenue because clearly we are going to face that as we go forward to advocate it here? This is a time of limited resources at the Federal level. People are worried about revenue losses. Is there any really credible authority that can test the notion that these zones have worked?

Mr. COWDEN. I think it is safe to say—and possibly telling to say—that we talked with hundreds of cities and States, and we have yet over several years to find one example of a city or a State that said, "Boy, we sure wish we hadn't gotten into this. The revenue loss is just killing us." The tendency seems to be if they get the new jobs and the new investment and the new development, the amount of tax revenue that they forego is a relatively minor consideration.

Senator LIEBERMAN. Mr. Butler or Mr. Woodson.

Mr. BUTLER. I think Dick Cowden really said it all when he said the jurisdictions that are taking the loss on the incentives almost with unanimity feel that it is well worth it. There is really a complete consensus or unanimity, on the idea that Enterprise Zones do work.

The debate you will have is over what kinds of Federal incentives will be most effective in spurring them along even faster, and that is a proper debate. But I do not know of any major attack on Enterprise Zones that has really been sustained.

Mr. WOODSON. There are some analogies to be drawn from the situation that we are now confronting with low income housing. We have about 1.4 million vacant privately owned housing—the Federal Government owns some—and maybe 80,000 vacant, unused public housing units laying fallow.

Today in my office the President of the Amoco Corp. in cooperation with the local low income housing group in Denver proposed to HUD to take ownership to purchase 200 of these houses in a low income area of Denver that are vacant—it is in the HUD inventory—for $10,000 each, and they were prepared to invest up to $20,000 each in these homes and then make them available to low- and moderate income people with incomes between $15,000 and $25,000.

The response from the local HUD office was to laugh at the offer because they said that these houses—the market value is $25,000 and therefore the Federal Government would lose. The houses have been on the market for 2 years, and they have been vacant. And every month they remain vacant, it's a drain on the tax dollars. Yet, bureaucrats resist any attempt to bring these houses even with a private group willing to invest money to fix them that will cause their value to exceed their fair market value. But that is the kind of thinking that we confront as we attempt to promote innovation in this area.

Senator LIEBERMAN. Let me bounce a few of the criticisms that are traditional that I have heard toward the program and see how you respond to it.

There was an article in the *New Republic* a while ago that was critical of Enterprise Zones. I think I am being fair if I say that one of the criticisms seemed to be that, well, what we ought to be doing is helping poor people, not poor places; in other words, that the Enterprise Zones held no real guarantee that poor people would be helped, just that businesses might relocate into what had been poor places. How do any of you respond to that?

Mr. BUTLER. That is a central question, of course, regarding any approach to try and revive any place. It is a debate that has been going on for many, many years. Do we help people or places?

I think those of us on this panel, and others who support Enterprise Zones, understand that the ultimate objective is to help people, not pieces of property. But we also recognize that people are parts of communities, and people live in places and do not want to move elsewhere. To simply say to them that we are only going to treat you as individuals, and we are going to ignore the fact that you are in a community with all kinds of disincentives and problems within it, is a very naive approach.

The Enterprise Zone strategy is based on the notion that people actually live in the South Bronx and elsewhere, and by addressing that community itself in a certain way, you by definition help the people within it as a result.

Senator LIEBERMAN. Do you think we should require that Enterprise Zones employ X percentage of their workforce from within the zone?

Mr. WOODSON. I think there should be in terms of targeting to give greater incentives for indigenous businesses. You can do that by perhaps placing some restrictions on the size of the businesses, giving additional incentives for indigenous businesses, providing information, also provide incentives for organizations that are nonprofit and others in the community that reduce crime in the community and improve the civil environment which enables businesses to flourish.

We do very little to talk about the civil environment. And there are many groups we have worked with that have improved the civil environment which allows business to flourish. And so, if we are talking about a strategy to revitalize the community, we have to take the social and economic elements of that as a part of the same strategy.

Mr. BUTLER. I agree with that, and as I said at the beginning of my testimony, I think it is very important we do not try to micromanage activity within these areas.

The fact is that small firms, particularly in very depressed areas, tend to recruit their employees locally who walk in off the street. They do not tend to advertise in the *Wall Street Journal.* And so, I think that if the Federal Government starts coming in and saying you'll hire this person and not that person, and so on, you will not get anyone opening a business in the first place. But if you have incentives, as Bob said, that focus on small firms and indigenous firms, in practice that will mean that there will be jobs created for people within that area itself.

Mr. WOODSON. Senator, just one other comment that your question raises, and that is that what we tend to do with low income communities is that—you know, there is an old adage, you get more of what you reward and less of what you punish. What we tend to do with poor people is only reward irresponsibility and failure.

We ignore the fact that half of the families living in low income communities children are not on drugs or dropping out of school or having daughters who are pregnant. And we do nothing for middle class people who happen to be poor, who happen to be low income living there. But they are adversely affected by the environment because of a lack of insurance that crime creates and the bad environment. So, what we should do—an Enterprise Zone, what it does, it treats both the people living there and the institution.

So, that is why I am a strong advocate by helping poor people, by enabling those who are living in the environment to have incentives for the healthy elements to have a positive effect on the unhealthy elements. And I call these community antibodies. And the most effective form of treatment of the human body is to provide assistance to the body's immune system. Well, these healthy elements in families living there represent the community's immune system, and I think we should do everything. An Enterprise Zone energizes the immune system and enables the body to heal itself. And, therefore, the institution is the way to go as well as the person.

Senator LIEBERMAN. Well said.

Senator Boschwitz.

Senator BOSCHWITZ. I would ask Mr. Woodson. Have you talked about that specific case to your friend, the Secretary, or is that something that just came up this morning?

Mr. WOODSON. It just came up today. I was going to bring this to the Secretary's attention because I know he would be outraged to know that this is happening.

But as you know, it takes a long time to turn around the bureaucracy. I have talked to people at the regional level, and the word is out there, well, Secretary Kemp, like other secretaries, will lose interest, and we are just going to conduct business as usual. No matter who he appoints, we will just conduct business as usual.

And they do not know the Secretary as we know him. And I know that once he finds out things like this, he is going to call his officials in the room and demand and explanation and move these barriers. And so, I will be bringing this to his attention.

But there are hundreds of groups out there, corporations like the Amoco Co. and others, who are willing to work with local housing groups that are producing and renovating housing if they can get a hold of this stock that HUD has. And the bureaucrats seem to be unwilling to release it even when the Federal Government is not asked to put up any money. None of these groups that I know of are asking the Federal Government to invest anything. They are merely saying let us purchase the properties from you that are in your inventory.

Senator BOSCHWITZ. Well, I suggest to you that you do. As I met the Secretary today, he right away asked where you were, and I know of his regard and admiration for you in what you have done

and what you are seeking to do. So, you have a friend there and you certainly should move forward with that.

I might tell you that I do disagree with you about set-asides. I have been involved in them. I have been involved with contractors in minority communities. There may be one who is making $1 million, and maybe the Set-Aside Program should no longer apply to him because maybe he is on his way to making $2 million. But I know of scores and scores of minority entrepreneurs who are benefiting from the Set-Aside Program who are just work-a-day types who have small businesses. I think that it is both a noble effort on the part of the Federal Government, and it is an effort that has had some success.

Mr. WOODSON. Senator, my comment was—as I said, I was not trying to in any way deride the program. I am merely saying I think it is being misapplied. When people stand up and say that we must have Set-Aside Programs as a strategy to address poverty, I think that it is just——

Senator BOSCHWITZ. It is part of the mix, though, isn't it?

Mr. WOODSON. Well, Senator, it would be interesting to look at who is receiving the money, how many minorities they employ. Many of them are signators.

At Ray Donovan's trial in New York, he was found not guilty on certain charges of having a black State representative set up a dummy corporation that enabled him to meet his minority quota. And the judge in the case, when they found him not guilty, said the practice of having a black as a signator on a set-aside so that a prime contractor can meet his or her quota is so commonplace that the application of it by Mr. Donovan is common practice. So, therefore, they will not find him guilty.

And I think the point is that it is being abused. It is being misapplied, and I think it is an inappropriate strategy to be applied to poverty. Contractors who receive set-asides—and I agree with you. They are noble people who really want to make a living, but they have to compete in the market. They cannot go down into a low income black area and hire kids who are in the under-class. They have got to hire from the same population as white contractors because they have to compete.

Senator BOSCHWITZ. Well, because of a recent Supreme Court decision, the State of Minnesota decided not to continue its Set-Aside Program, it would conduct studies, and so forth. There was quite a hue and cry. A number of people got together through a meeting I organized. They may not have all hired only minorities, but there was no question that some pretty small businessmen were there, and not one or two, but scores. And they felt keenly that they had been advantaged and that they were threatened by the lack of these set-asides.

Mr. WOODSON. Sure.

Senator BOSCHWITZ. So, I think that the effort, not necessarily the people, is a noble one, and it should be continued. But I agree with you that it should not be thought of as the answer.

Let me ask you if you have a specific example of an Enterprise Zone working that you can, for the record, discuss that has been within the jurisdiction that you have worked in.

Mr. WOODSON. The only ones are the same ones that Congressman Jack Kemp talked about, and that is in——

Senator BOSCHWITZ. Newark?

Mr. WOODSON [continuing]. Newark, NJ. where a number of businesses were able to come in and function. But unfortunately, a lot of the low income communities where the National Center operates, they do not have Enterprise Zones, and that is why I am here testifying in support so that the Cochran public housing that was profiled on "60 Minutes" should be declared an Enterprise Zone. The far northeast where we are currently working in setting up a mini-mall inside of a shopping center so that young people living there can learn the free enterprise system—that should be declared an Enterprise Zone. So, I do not have direct experience. Stuart and others around the country have.

Senator BOSCHWITZ. Well, I am going to get to Mr. Butler and Mr. Cowden. I'll go then on to Mr. Butler.

Do you think that the Administration's bill does not—is it just a good start? Is it an adequate start? Is it fatally flawed? Should it do more? You talked about Enterprise Zones that are already existing. If it is incorporated with some advantages that are given there, will this be enough of an added incentive to spur growth within Enterprise Zones?

Mr. BUTLER. I would call it an adequate start. And I know there are those who say that we should maybe delay this legislation, perhaps delay adding it to reconciliation, in order to get a better package next year. I have heard that for 10 years. Indeed, I probably said it myself in some of the early years.

What I feel now is let us get a Federal program started, even if it does not do all that many of us would want it to do. As I said, I have suggested some ways of strengthening the legislation, and I would certainly urge this Committee and others to push for an enhancement in those areas. But when it comes to the bottom line, I do think it would be wiser to push hard to get something through this year than to delay it again. I think the momentum is up, and let's just go with it.

Senator BOSCHWITZ. We are going to look at that. The Chairman asked me if we should put this on the reconciliation bill, and I said I was part of a movement to strip everything off the reconciliation bill.

Mr. BUTLER. I do understand that, sir.

Senator BOSCHWITZ. However, one feels that if you are not successful, you may as well get your own piece on there as well. So, we will see how that goes.

Mr. Cowden, you are the executive director of the American Association of Enterprise Zones. I was hopeful that you would tell us what precisely is working. I was hopeful that you would say that in Boston there is an Enterprise Zone. It is 8 square blocks or 12 square miles. In Atlanta it is this, or wherever. Can you give us some examples and tell us what incentives most specifically are working the best?

Mr. COWDEN. Yes. I cannot emphasize enough how often we find that the most successful Enterprise Zones are those that are basically an extension of the local community's overall redevelopment program. By this I mean programs that include tax incentives, but

that also include a comprehensive program to actually fix the things that are wrong with those neighborhoods—the streets, the sewers, the bridges, the sidewalks. Let me give you a good example of how this can work and has worked successfully.

In Trenton, NJ—in fact, the entire New Jersey program is innovative in having a kind of incentive that is both a tax incentive and a form of direct assistance.

The State of New Jersey has a 6 percent sales tax. Any qualified business—any business within an Enterprise Zone—can charge only 3 percent. The state then takes the 3 percent that they collect in their normal sales and turns that into a cash assistance fund that is then sent back to the communities with the proviso that they have to use it to make improvements in the zone.

In Trenton, they have used that. I have seen it myself. They have used it very successfully to relight city streets that were so dark that people would not come shop there. They have used it to fix the streets. They are using it for public works projects over and above what their budgets would normally allow.

So, you get a double bang here. You get both the tax incentive benefit for the local businesses and you have a source of revenue to make improvements in these areas which are old and decaying. If I could point to a form of the program that works best, this is it.

I would go a step further to say that we are beginning to think more about this question of using the State program as a means of providing direct assistance rather than devoting as much attention to tax incentives. State tax incentives have a limited potential simply because the typical company pays less than 5 percent of its annual revenues in State taxes. So, even if you wipe out all State taxes, you are only affecting a relatively small element of their decisionmaking.

Senator BOSCHWITZ. I am a businessman. I am waiting for somebody to say something about real estate tax. I have always thought as I looked at these type of bills that there should be some emphasis laid on taxes that are going to occur, most specifically real estate taxes or in this case sales taxes that are going to be part of every transaction, that are going to be part of every business.

Have local communities and counties also chipped in, so to speak?

Mr. COWDEN. Yes, they have. And I am not saying that real estate taxes should never be a consideration. Certainly if everybody is defaulting on their property taxes, the local community is not gaining much in terms of real estate tax revenue anyway. So, there is very little percentage in even charging real estate taxes in areas that are that profoundly affected.

What I am saying, though, is that the typical kind of situation that you have in Enterprise Zones is that they are competing to get new businesses of all kinds, small and medium and large, with suburban communities and communities that have new infrastructure or that are in good locations. And when companies are going through a decisionmaking matrix and trying to figure out where they are going to locate a new branch or a new office, the factor of whether they are going to pay a marginal State tax can sometimes tip the decision in favor of an Enterprise Zone.

But more than likely the considerations that they are really making are, "Are my employees going to be safe? Can I get my goods in and out of the place? What are the streets like? Is the bridge washed out?" Those are infrastructural questions. And I think that those are the things that the cities and States should be looking at. I think that should be the major part of their program.

I think the Federal tax incentives can induce them to do more of that kind of thing. I do not think that the Federal program has to be a spending program. We do not have to have urban renewal revisited in order to have Enterprise Zones, but I think that the cities and States would compete by spending more of their resources on these very necessary and mundane kinds of things that have to be present in order to have redevelopment if they think that they have an opportunity to be able to offer basically as part of their portfolio of incentives the kinds of things that are in Mr. Kemp's proposal. I think that there can be an interaction between those two kinds of programs.

Senator BOSCHWITZ. Thank you.

Senator LIEBERMAN. Thank you.

Senator Burns.

Senator BURNS. I have just a couple of questions. Are you familiar with the incubators? Does this relate, Mr. Cowden, or are you familiar with that?

Mr. COWDEN. Oh, yes. We have seen—in fact, we did film once on the incubator in Baltimore, in the Hyde Park district of Baltimore. It was a very successful program.

Again, when you have an area where there is kind of a sense of—that any small business that opens up a storefront operation in an area where everything is closed down around them and boarded up and there is litter and that sort of thing, their chances of independent success diminish. But in the Baltimore situation, their incubator, they have a number of flourishing small operations that are providing jobs in those neighborhoods and providing entrepreneurial opportunities.

I think that incubators are uniquely appropriate to Enterprise Zones.

Mr. BUTLER. Maybe I could just add something to that. I think that the Enterprise Zone is related to a number of things, a number of approaches, the incubators being one. These all share the characteristic of people setting up new enterprises that create wealth and create jobs. Thus the Enterprise Zone is related to incubators.

It is also related to many of the things that Bob Woodson is doing, such as tenant management of public housing. We see here in the District, for example, a tenant management group starting businesses. It is to try and create an atmosphere to encourage and to reward that kind of creativity, whether it be incubators or tenant management or whatever, that the Enterprise Zone is designed to do. It should not try to steer people into particular activities, however, or to give special favors to one particular venture, rather than another. It should be an overall framework in which incubators and other approaches can flourish better than they would do without that basic foundation.

Senator BURNS. You are saying in this case, though, that what has been recommended here in these Enterprise Zones would facilitate those establishments.

Mr. BUTLER. Absolutely, it would.

Senator BURNS. Would it be a secondary to it or would it be a primary movement?

Mr. BUTLER. I think it is a climate-setting element, much like the general tax code is for business creation. In the case of the general tax code, cutting taxes generally spurs all kinds of creative enterprises and various approaches that use tax incentives. I think that is analogous in the case of the inner city. In practice you would see incubators tending to flourish in Enterprise Zones. I think they are the kinds of activities and facilities that would be appropriate in those areas.

Senator BURNS. Do we get into a situation when we establish Enterprise Zones that we take—do new businesses take advantage of that situation and move into those zones and you lose them in other areas, and the attitude of maybe an existing business in competition is saying, OK, they are operating in this zone here, and that is kind of unfair competition? We have everything else going. How do you address those situations?

Mr. COWDEN. Let me point out just from the real world situation. I can't remember. I think it was the Penn State study or the New Jersey study that found that less than 9 percent of all new businesses in the zones were relocations.

The typical scenario again is trying to level out the playing field here where the playing field has been very much in favor of the suburban areas that are brand new and have all the natural locational advantages. We do not find that a company is going to—the company that is making a profit and is a sound operation is going to pick up roots to move from the suburban site into an Enterprise Zone just to get a tax incentive. That is not going to happen even with the Federal program.

We have actually seen that raised as kind of a red herring by the critics who say, on the one hand, we do not think Enterprise Zones are going to work, and if they do, they are going to rob businesses from places where they are existing already. You cannot have it both ways. It does not work that way.

Mr. BUTLER. I might add, Senator, the spillover effect cuts two ways. You no doubt could find in some of the small business organizations somebody who will say, "what about the business on the other side of the street from the zone." There is this image that somehow such a business by definition is losing as a result of an Enterprise Zone.

But, of course, what one tends to find in poor neighborhoods is that when an area is blighted and decaying, it pulls down neighborhoods around it. People who are located close to high crime, high unemployment, declining neighborhoods suffer problems in their business. An Enterprise Zone reverses the spiral, and I believe very strongly that the impact of creating an Enterprise Zone in the middle of the South Bronx would very much be to the benefit of those businesses a few blocks away from that zone who are also in the South Bronx. You would lift everybody up. It would be a posi-

tive spillover just, as a declining neighborhood is a negative spillover.

So, I would to worry too much about the fear that an Enterprise Zone is going to rob Peter just to pay Paul.

Mr. WOODSON. The nature of low income environments tend to be self-selecting with regard to business location. And I can just draw an example from Senator Kerry's area.

We have a very active resident management program in Jamaica Plains in Boston in Bromley-Heath. Now, prior to the residents taking over the management of that development, you had 3,000 broken windows. Jordan-Marsh, Sears, none of these stores would ever make deliveries there and there were no indigenous businesses. And the police would not patrol after 5 o'clock. But after the residents took it over and reduced crime and the fear of crime, all of the businesses began to make deliveries. The phone companies could pick up their telephones—utility companies. Allstate lost fewer cars and what have you.

So, it was an overall improvement. So, it enabled small businesses developed by the residents themselves to develop and flourish too. So, it really benefited all parties. Other businesses serving the zone would benefit because they now will expand their business opportunities, but it also helps indigenous businesses as well. So, it is seldom either/or; it is both/and.

Senator BURNS. Well, like I say, even though we come from a rural area—and I guess I am very supportive of this thing because like I say, we have a hard time understanding the problems in the inner cities where we are beings we don't even have cities much. In fact, out in our part of the country, we do not have rush hours, we have rush minutes. [Laughter.]

Some way or another I think we can apply this to some of the situations that we have existing in our rural communities where we have a labor force, but we do not have a vehicle really to start something out. And I think we will do that.

I want to thank all three of you for your testimony. It has been very informative to me. And, Mr. Woodson, you are doing the Lord's work, and I applaud you for that.

Mr. WOODSON. Thank you.

Senator LIEBERMAN. Thank you, Senator Burns.

Just one final question from me for Mr. Cowden, really a structural question.

At the hearing we had in June one of the State officials suggested that the Federal Government essentially contract out the administration of a Federal Enterprise Zone Program to the States who are operating them now. What do you think about that?

Mr. COWDEN. I love that idea. Let's put it this way. They have plenty of experience in the job. They have been doing this for a long time.

Really we do not want to see Enterprise Zones become—again, I'll use the word urban renewal—a version of urban renewal. We think that the administration, the decisionmaking, and so forth, belong at the State and local level. These people basically know what they are doing.

If we could have a Federal program that simply reinforced what they are doing, and let them know that they have Federal backing

and additional Federal incentives, again I think that they would do more than they are doing now.

Senator LIEBERMAN. I appreciate that.

Unless anybody is burning with another statement to make, we have come to right about the point where we thought we would adjourn.

I think it has been an excellent hearing both in terms of the enthusiasm for the idea, but also the very specific experiences and suggestions that you have brought to bear. Mr. Woodson, Mr. Butler, and Mr. Cowden, I thank you very much. And I hope from this can come some real action on Enterprise Zones in this session of Congress.

The hearing is adjourned.

[Whereupon, at 3:28 p.m., the Committee was adjourned.]

APPENDIX

U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OFFICE OF CHIEF COUNSEL FOR ADVOCACY

STATEMENT OF

HONORABLE SUSAN S. ENGELEITER

ADMINISTRATOR

U.S. SMALL BUSINESS ADMINISTRATION

BEFORE THE

SENATE SMALL BUSINESS COMMITTEE

SEPTEMBER 21, 1989

(225)

Good afternoon Mr. Chairman and Members of the Committee. Thank you for your interest in learning the views of the U.S. Small Business Administration on enterprise zones; I appreciate the opportunity to discuss their importance to small business. It is my firm belief that the small businesses of our Nation must be major participants in successful economic development and job creation activities.

I would like to state at the outset that the SBA has consistently supported the enterprise zone concept, and it continues to do so. As you know, President Bush has submitted an enterprise zone proposal to the Congress which contains tax-based incentives for new enterprises and new jobs in distressed urban and rural areas. I commend Senators Boschwitz and Danforth, as well as their colleagues in the House, for introducing these proposals. Following enactment of this legislation, we look forward to working with Congressional and Administration officials to develop successful federal enterprise zones.

We at SBA are committed to economic development. The establishment of enterprise zones is an integral tool in this effort. Since 1982, 37 states and the District of Columbia have established enterprise zone programs. According to the May 1989 issue of Business Facilities magazine, these state programs have stimulated the creation of more than 184,000 new jobs, as well as helped retain nearly 169,000 existing jobs. As important evidence suggests the state zones have stimulated more than $18 billion in

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capital investment. The federal government can enhance the potential of state enterprise zones by further encouraging neighborhood stabilization and entrepreneurship, particularly through small business participation.

Simultaneously, enterprise zones have benefitted small businesses. According to a 1985 study prepared for the U.S. Small Business Administration and a 1986 U.S. Department of Housing and Urban Development report, urban enterprise zones have produced a positive impact on business investment; they are serving a vital role as a catalyst for local business activity. According to the HUD study, the enterprise zone program functions in most places as a program for small businesses, and small firms account for most new zone activity.

- Only four percent of the 263 firms known to have invested in the ten zones surveyed had more than 200 employees; only ten percent had more than 100 employees; 63 percent of the businesses claimed fewer than 50 people, and many of those firms were very small.

- In only one of the states examined (Florida) were large firms expressly targeted for the principal state zone incentives.

- Even in Connecticut, where the incentive package appears geared to larger operations, zone enterprises tend to be smaller rather than larger firms.

- Some small business owners surveyed indicated that the enterprise zone program offered them access to local government that tended to come automatically to larger concerns.[1]

As Secretary Kemp has stated, enterprise zones are designed to foster an investment climate that will create new jobs and help produce new entrepreneurs in distressed areas. Policies to facilitate enterprise zones should be those that promote the formation and expansion of small business. Small businesses are the primary job generators in the U.S. economy, creating two-thirds of the new jobs between 1980 and 1986. Small firms consistently create the majority of new jobs, especially during economic downturns. Additionally, small businesses and self-

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[1]Susan A. Jones, Allen R. Marshall and Glen E. Weisbrod, Business Impacts of State Enterprise Zones (Cambridge, Massachusetts: prepared for the U.S. Small Business Administration by Cambridge Systematics, Inc., September 1985): HUD, Office of Program Analysis and Evaluation, State-Designated Enterprise Zones: Ten Case Studies (Washington D.C.: U.S. Government Printing Office, August 1986).

employed entrepreneurs represent 56 percent of U.S. private employment and 47 percent of the Nation's output. So, it is natural to look to small business to stimulate economic growth in both urban and rural areas.

I would like to give you just two examples of the importance of small business in enterprise zones. The City of San Jose, California, on May 1, 1989, launched a $50 million program within an enterprise zone to help mom-and-pop shops and modest entrepreneurs. Advocates of the new loan program, which is expected to generate $50 million within five years, say current market conditions are insufficient to assist many small businesses. Often smaller operations are wary of bankers and banks often try to avoid the up-front costs of processing small loans. San Jose's director of economic development is very enthusiastic about the loan program because it will allow participating banks to comply more easily with a federal law that requires federal lending institutions to write off a portion of their loans in their communities. The economic development director considers this a fair system in which applications will be rotated from bank to bank.

The Park Circle Enterprise Zone in Baltimore, Maryland, another enterprise zone which emphasizes the value of small business ownership and entrepreneurship, is prospering. Ten million dollars in state and city money have been spent for the

industrial park, which opened in 1982. Enterprise zone businesses now have more than 1,000 employees. A Control Data Corporation owned small business incubator has spawned more than 150 firms.

With respect to the proposed enterprise zone program, you asked me to comment on targeted regions, tax incentives for small business owners, and the impact on jobs.

I strongly recommend competitive selection of enterprise zones; zones should be located in areas that promise enthusiastic support. States and localities which offer a comprehensive package supporting enterprise zones should be given preferential treatment. This package could include such items as relief from land use regulations, building codes, rent control, and zoning laws. Child care assistance, effective job training programs, anti-drug and crime prevention measures, as well as other employee and community efforts, should be encouraged.

I support Senator Danforth's effort to set aside a certain portion of the enterprise zones for rural areas. The shift in the focus of American industry - from predominately resource extraction and manufacturing industries to service or information based industries - has created economic difficulties for rural communities tied to old resource based industries. In the last eight to ten years the United States has created 15 million new

jobs; however, this is largely an urban phenomenon. In rural areas, small firms are not contributing new jobs at the same rate as in urban areas. Between 1976 and 1984, the number of jobs in firms with fewer than 500 employees grew only 23 percent in rural areas, as opposed to 31 percent in urban areas. Since many states have already demonstrated that enterprise zones are an important economic development tool, I think it is important to have successful rural models.

Tax incentives may encourage entrepreneurship. The President's proposed refundable tax credit for low-income zone employees should help entrepreneurs secure an adequate workforce.

The President's proposal benefits both enterprise zones companies and the investors in those companies. For investors, the proposal would permit investors to take as a deduction $50,000 a year of their investments in qualified companies up to a lifetime maximum of $250,000. For corporations, certain capital gains from the sale of tangible trade or business property located in the zone for two years or more will not be taxed.

As the Congress deliberates on enterprise zone and other economic development proposals, I urge you to consider Federal policies which serve as "domestic barriers" to international competitiveness and economic development. These policies tend to be those that impose disproportionate regulatory burdens on small

firms, restrict the ability of a small business to react quickly to changing markets or to increase employment. Thus, current Congressional debates on mandated health benefits, family leave, and minimum wage all have important small business implications. At the same time, I am concerned about inaction on needed reforms such as uniform product liability laws.

Again, let me assure you of the firm commitment of the U.S. Small Business Administration to the enterprise zone program. We look forward to working with you in full cooperation and partnership.

Thank you for this opportunity. I will be pleased to respond to your questions.